Appendix B

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on behalf of himself and all others similarly situated

represented by

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V.

Defendant
Merrill Lynch, Pierce, Fenner & Smith, Inc.
a corporation

represented by

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Appendix B

Date Filed	**Docket Text**
10/23/2002	CERTIFIED TRUE COPY OF CONDITIONAL MDL TRANSFER IN ORDER FROM THE MDL PANEL . . . transferring action from the U.S.D.C. for the Western District of Oklahoma, Docket No.: 5:02-cv-564, MDL No.: 1484,, to the S.D.N.Y. Mailed letter requesting transfer of their file. (jol) (Entered: 10/28/2002)
	* * *
11/10/2002	MDL TRANSFER IN: Received certified copy of docket entries and file from the District of Western District Oklahoma, Docket No.: 5:02cv564(SPF), MDL No.: 1484. (gmo) (Entered: 11/19/2002)
	* * *
02/07/2003	NOTICE OF MOTION by Merrill Lynch, for an Order pursuant to FRCP 12(b)(6) dismissing the complaints for failure to state a claim upon which relief may be granted . Return Date 4/10/03 at 10:30 a.m. Exhibits A through D are attached. ORIGINAL ENTERED IN CASE #02 MDL 1484 (MP), DOC. #174. (tp) (Entered: 03/05/2003)

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02/07/2003	MEMORANDUM OF LAW by Merrill Lynch in opposition to the remand motions of Ciccarelli, IJG Investments, and Smith and in support of their [0-1] motion for an Order pursuant to FRCP 12(b)(6) dismissing complaints for failure to state a claim upon which relief may be granted. (tp) (Entered: 03/05/2003)
03/12/2003	MEMORANDUM OF LAW AND RESPONSE AND OBJECTION by Shadi Dabit re: [0-1] motion for an Order pursuant to FRCP 12(b)(6) dismissing the complaints for failure to state a claim upon which relief may be granted . (yv) (Entered: 03/13/2003)
04/10/2003	OPINION AND DECISION # 88340, denying [0-1] motion for an Order pursuant to FRCP 12(b)(6) dismissing the complaints for failure to state a claim upon which relief may be granted; the motions to remand the Ciccarelli, IJG Investments, and Smith actions are denied . (signed by Judge Milton Pollack); (Orig. doc. filed in case 02 MD 1484, Doc. #222) (ae) (Entered: 04/10/2003)
05/09/2003	NOTICE OF APPEAL by Shadi Dabit from [0-1] order the motions to remand the Ciccarelli, IJG Investments, and Smith actions are denied . Copies of notice of appeal mailed to Attorney(s) of Record: Skadden, Arps, Slate, Meagher & Flom, LLP,

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	Seeger Weiss, LLP, Trujilo, Rodriguez & Richards, LLC, Schoengold & Sporn, P.C. and Kaplan, Fox & Kilsheimer, LLP. $105.00 Appeal filing fee paid 5/14/03 on receipt # E 473580. (dt) (Entered: 05/14/2003)
05/14/2003	Notice of appeal and certified copy of docket to USCA: [3-1] appeal by Shadi Dabit ; Copy of notice of appeal sent to District Judge. (dt) (Entered: 05/14/2003)

* * *

07/31/2003	JUDGMENT; that for the reasons stated in the Court's Opinion (88340) and Order dated 4/10/03, defendant's motions to dismiss all the complaints are granted and the motions to remand the Ciccarelli, ILG Investments, and Smith actions are denied. (signed by J. Michael McMahon, Clerk of Court); Entered On Docket: 8/7/03. (ae) (Entered: 08/07/2003)

* * *

08/26/2003	Transcript of record of proceedings before Judge Milton Pollack on 4/10/03. (kw) (Entered: 08/26/2003)

* * * *

APPENDIX C — RELEVANT DOCKET ENTRIES OF THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA (OKLAHOMA CITY)

U.S. District Court
Western District of Oklahoma[LIVE] (Oklahoma City)
CIVIL DOCKET FOR CASE #: 5:02-cv-00564

Dabit v. Merrill Lynch Pierce	Date Filed: 04/26/2002
Assigned to:	
Honorable Stephen P. Friot	Jury Demand: Both
Demand: $75,000	Nature of Suit: 190
Cause: 28:1332	Contract: Other
Diversity-Other Contract	Jurisdiction: Diversity

No. 5:02-cv-00564

SHADI DABIT,
on behalf of himself and all others similarly situated,

Plaintiff,

v.

MERRILL LYNCH, PIERCE, FENNER & SMITH, INC.,
a corporation,

Defendant.

Appendix C

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on behalf of himself and all others similarly situated

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V.

Defendant
Merrill Lynch Pierce Fenner & Smith Inc
a corporation

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Appendix C

Date Filed	Docket Text
04/26/2002	COMPLAINT (eh) (Entered: 04/29/2002)
	* * *
05/16/2002	OPPOSED MOTION by defendant Merrill Lynch Pierce to extend time to answer or otherwise respond to plf's class action compl (ap) (Entered: 05/17/2002)
05/17/2002	ORDER by Honorable Stephen P. Friot granting dft's motion to extend time until 7/18/02 to answer or otherwise respond to plf's class action compl [7-1] (cc: all counsel) [EOD Date 5/17/02] (ap) (Entered: 05/17/2002)
05/17/2002	OPPOSITION by plaintiff Shadi Dabit to dft's motion to extend time to answer or otherwise respond to plf's class action compl [7-1] (ap) (Entered: 05/17/2002)
05/20/2002	COMBINED MOTION by plaintiff Shadi Dabit to reconsider order granting enlargment of time to answer and Brief in Support (nm) (Entered: 05/21/2002)
05/22/2002	ENTER ORDER by Honorable Stephen P. Friot re [10-1] a hrg on Plf's Motion to Reconsider Order Granting Enlargement of Time to Answer is hereby set for Friday

5/24/02 @ 3:00 pm before Judge Friot ctrm #401 (cc: all counsel) [EOD Date 5/22/02] (nm) (Entered: 05/22/2002)

* * *

05/28/2002 ENTER ORDER by Honorable Stephen P. Friot GRANTED motion to reconsider order granting enlargment of time to answer [10-1] The court reaffirms its Order of 5/17/02. The court waives the Rule 26 provision barring disc prior to a disc conf, to the following extent only: Plf is authorized to serve a Rule 34 doc request on Dft at any time hereafter, if Plf desires to do so. Dft's responses to any such Rule 34 doc request shall be due not later than 7/18/02 (cc: all counsel) [EOD Date 5/28/02] (nm) (Entered: 05/28/2002)

06/10/2002 MOTION by plaintiff Shadi Dabit for particularized expedited discovery fm third-pty witnesses to preserve evidence and brf in supp (ap) (Entered: 06/11/2002)

06/27/2002 NOTICE of Filing with the Judicial Panel on Multi-District Litigation Motion to Stay Proceedings by defendant Merrill Lynch Pierce (ap) (Entered: 06/28/2002)

06/27/2002 MOTION by defendant Merrill Lynch Pierce to stay proceedings (ap) (Entered: 06/28/2002)

* * *

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06/28/2002	OPPOSED MOTION by defendant Merrill Lynch Pierce for enlargement of time to resp to plf's mtn for particularized expedited discovery fm 3rd-pty witns to preserve evidence and brief in supp (ap) (Entered: 06/28/2002)
07/02/2002	ORDER by Honorable Stephen P. Friot granting dft's motion for enlargement of time to resp to plf's mtn for particularized expedited discovery fm 3rd-pty witns to preserve evidence [17-1] Response due 7/9/02 (cc: all counsel) [EOD Date 7/2/02] (cjs) (Entered: 07/02/2002)
07/05/2002	DOCKET status/scheduling ; status scheduling conf set for 1:30 8/6/02 (cjs) Modified on 07/31/2002 (Entered: 07/05/2002)
07/05/2002	RESPONSE by plaintiff Shadi Dabit to motion to stay proceedings [15-1], motion for particularized expedited discovery fm third-pty witnesses to preserve evidence [14-1] (cjs) (Entered: 07/08/2002)
07/08/2002	ORDER by Honorable Stephen P. Friot denying dft's motion to stay proceedings [15-1], denying dft's Notice of Filing with the Judicial Panel on Multi-district Litigation/notice [15-1] (cc: all counsel) [EOD Date 7/8/02] (cjs) (Entered: 07/08/2002)

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07/09/2002	OBJECTION by defendant Merrill Lynch Pierce to plf's motion for particularized expedited discovery fm third-pty witnesses to preserve evidence [14-1] and brief in support (ap) (Entered: 07/10/2002)
07/10/2002	ORDER by Honorable Stephen P. Friot denying motion for particularized expedited discovery fm third-pty witnesses to preserve evidence [14-1] (more fully set out) (cc: all counsel) [EOD Date 7/10/02] (fp) (Entered: 07/10/2002)
07/11/2002	RENEWED MOTION by defendant Merrill Lynch Pierce for stay of proceedings pending mtn bef the Judicial Panel on MDL, or in the alternative, an extension of time to coordinate the response (ap) (Entered: 07/12/2002)
07/12/2002	SUPPLEMENT by defendant Merrill Lynch Pierce re renewed motion for stay of proceedings pending mtn bef the Judicial Panel on MDL [23-1], or in the alternative an extension of time to coordinate the response [23-2] (ap) (Entered: 07/15/2002)
07/15/2002	ENTER ORDER by Honorable Stephen P. Friot bef the Ct is dft's renewed mtn to stay of proceedings pending mtn bef the Judicial Panel on MDL or in the alternative an ext of time to coordinate resp, filed on 7/11/02 and

dft's suppl to the renewed mtn filed on 7/12/02; the request for an extension of time to answer [23-2] is DENIED; the Ct will address the renewed mtn for stay after plf has responded to the mtn; plf's response is due by 7/29/02 (cc: all counsel) [EOD Date 7/15/02] (ap) (Entered: 07/15/2002)

07/18/2002 MOTION by defendant Merrill Lynch Pierce to dismiss complaint and memorandum of law (ap) (Entered: 07/19/2002)

07/23/2002 COMBINED MOTION by plaintiff Shadi Dabit to compel dft to respond to discovery requests and brief in support (ap) (Entered: 07/23/2002)

07/25/2002 MOTION by defendant Merrill Lynch Pierce to stay discovery , and for protective order and brf in supp (ap) (Entered: 07/26/2002)

07/29/2002 RESPONSE by plaintiff Shadi Dabit to dft's renewed motion for stay of proceedings pending mtn bef the Judicial Panel on MDL [23-1] or in the alternative, an ext of time to coordinate response (ap) (Entered: 07/30/2002)

07/31/2002 ENTER ORDER by Honorable Stephen P. Friot all pending motions in this matter re [28-1], [28-2], [27-1], [23-1], other than the motion to dismiss, are set for hearing;

hearing set on 8/16/02 at 8:30 am; pending that hearing, all discovery proceedings and discovery activity in this action are stayed (cc: all counsel) [EOD Date 7/31/02] (ap) Modified on 09/18/2002 (Entered: 07/31/2002)

* * *

08/05/2002 RESPONSE and Ojbection by plaintiff Shadi Dabit to dft's motion to dismiss complaint [26-1] (ap) (Entered: 08/06/2002)

* * *

08/08/2002 MOTION by defendant Merrill Lynch Pierce for leave to file reply brf (ap) (Entered: 08/09/2002)

08/09/2002 ORDER by Honorable Stephen P. Friot granting dft's motion for leave to file reply brf [34-1]; the Ct grants dft 10 days fm the date of this order to file reply brf not to exceed 10 pgs in length (cc: all counsel) [EOD Date 8/9/02] (ap) (Entered: 08/09/2002)

08/12/2002 RESPONSE by defendant Merrill Lynch Pierce to plf's motion to compel dft to respond to discovery requests [27-1] (ap) (Entered: 08/13/2002)

* * *

Appendix C

08/14/2002	MOTION by plaintiff Shadi Dabit for leave to reply to Dft's response to Plfs motion to compel (nm) (Entered: 08/14/2002)
08/15/2002	ORDER by Honorable Stephen P. Friot granting pla's motion for leave to reply to Dft's response to Plfs motion to compel [38-1] pla may file reply to dft's mtn to compel w/in 5 days of the date of this order (cc: all counsel) [EOD Date 8/15/02] (cjs) (Entered: 08/15/2002)
08/15/2002	REPLY by plaintiff Shadi Dabit to response to motion to compel dft to respond to discovery requests [27-1] (kw) (Entered: 08/16/2002)
08/19/2002	REPLY by defendant Merrill Lynch Pierce to plf's response to dft's motion to dismiss complaint [26-1] (ap) (Entered: 08/20/2002)
09/16/2002	MOTION HEARING COURTROOM MINUTES: Before the Honorable Stephen P Friot; plf's cnsl William Federman, Clell Cunningham; dft's cnsl Bruce Day, Bill Guest; the Court takes under advisement re [28-1], [28-2], [27-1], [23-1] (ap) (Entered: 09/16/2002)
09/18/2002	ORDER by Honorable Stephen P. Friot the renewed motion for stay [23-1] is DENIED; the July 25, 2002 motion to stay discovery

[28-1], [28-2] is DENIED, however, discovery is stayed until the status and sched conf to be held October 4; the motion to compel [27-1] is GRANTED; the timing of document production will be discussed at the October 4, 2002 status and sched conf (cc: all counsel) [EOD Date 9/18/02] (ap) (Entered: 09/18/2002)

* * *

10/09/2002 ORDER by Honorable Stephen P. Friot although the Ct suggested in its September 18 order re [43-1] that it would proceed to determine the timing of document prod, the Ct has, upon further consideration, concluded that all matters w/respect to discovery, including determination of the timing of doc prod, should await the Ct's ruling on the mtn to dism; if the mtn is granted, discovery matters will be moot; if it is not granted, the proper course will likely be much easier to determine; accordingly, the stay of discovery previously ordered by the court shall remain in place until the court rules on the pending mtn to dism (cc: all counsel) [EOD Date 10/9/02] (ap) (Entered: 10/09/2002)

10/11/2002 ORDER by Honorable Stephen P. Friot GRANTS motion to dismiss complaint [26-1] dismissing the complaint [1-1] Plf's

is granted lv to file an amended cmp w/i (10) days after the date of this order. In the amended cmp, plf is at liberty to plead any conbination of state and fed clms, in the alternative or otherwise, but state clms must be differentiated fm federal clms, in terms of the substantive bases for liability and in terms of causation and damges. (cc: all counsel) [EOD Date 10/11/02] (fp) (Entered: 10/11/2002)

10/21/2002 NOTICE to the Court of Transfer Order entered by Judicial Panel on MDL by defendant Merrill Lynch Pierce (ap) (Entered: 10/22/2002)

10/21/2002 FIRST AMENDED CLASS ACTION COMPLAINT by plaintiff Shadi Dabit; jury demand (ap) (Entered: 10/22/2002)

* * *

11/04/2002 TRANSFER ORDER, by Wm Terrell Hodges, Chairman, that pursuant to 28 USC 1407, the actions listed on the attached Sched A and pending outside the SD/NY are transf to the SD/NY and w/consent of that court, assigned to the Honorable Milton Pollack for coordinated or consolidated pretrial prcdgs with the actions pending there; Case transferred to the: SD/NY (cc: all counsel) [EOD Date 11/4/02] (ap) (Entered: 11/04/2002)

* * * *

APPENDIX D — CLASS ACTION COMPLAINT DATED APRIL 26, 2002

UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA

Case No. CIV 02-564-F

SHADI DABIT,
on behalf of himself and all others similarly situated

Plaintiff,

v.

MERRILL LYNCH PIERCE FENNER SMITH, INC., A CORPORATION

Defendants.

CLASS ACTION COMPLAINT

Plaintiff makes the following allegations upon information and belief except as to allegations specifically pertaining to plaintiff and his counsel, based on the facts alleged below, predicated upon the investigation undertaken by plaintiffs counsel, Plaintiff believes that further substantial evidentiary support will exist for the allegations set forth below after a reasonable opportunity for discovery.

Appendix D

NATURE OF THE ACTION

1. This is a class action brought by plaintiff on behalf of himself and all other former or current account executives ("Brokers"), who, while employed by Defendant, Merrill Lynch Pierce Fenner & Smith, Inc. ("ML") purchased one or more of the ML recommended securities identified in *Exhibit A*, attached hereto (the "ML Stocks"), individually or on behalf of Brokers' clients at any time during the period from December 1, 1999 through December 31, 2000 (the "Class Period"), and who suffered damages as a result of owning and holding such ML Stocks during this time period, or who suffered damages as a consequence of the loss of clients due to ML's wrongful actions.

2. Plaintiff alleges that ML, after Plaintiffs purchase of the ML Stocks, individually or on behalf of clients of Plaintiff, failed to advise Plaintiff of the fact of the decreasing values of the ML Stocks, and misrepresented to Plaintiff that the ML Stocks were worthy of holding in Plaintiffs or Plaintiff's clients' portfolio, all in violation of ML's fiduciary duty to Plaintiff and in violation of ML's covenant of good faith and fair dealing.

3. When the true value of the ML Stocks became apparent and clients of Plaintiff terminated their relationship with Plaintiff, Plaintiff suffered damages in the form of lost commissions that would otherwise have been earned from future business with such clients.

4. Throughout the Class Period the price of the ML Stocks promoted by ML were artificially inflated as a result of the

manipulative efforts of ML. As a result of the efforts of ML and its agents, employees and affiliates, ML was able to, and did, manipulate the price of the ML Stocks, causing these stocks to trade at artificially inflated prices throughout the Class Period.

5. Further, after regulatory authorities in the State of New York initiated investigations concerning ML's conduct, in June, 2001, and as pressure from those investigations increased, ML ceased manipulating the price of various stocks, and, as a result, the price of certain stocks steadily declined, leaving Plaintiff and clients of Plaintiff who purchased these stocks at manipulation-inflated prices with substantial losses. ML failed to advise Plaintiff of the fact of the investigations and the certain subsequent decline in the ML Stocks' values, thereby preventing Plaintiff from selling his personally held stocks at a minimal loss, and further preventing Plaintiff from advising his clients to similarly sell such ML Stocks in their individual portfolios.

6. ML, acting as a central nerve center in the manipulation of various stocks identified by the New York Attorney General ("NYAG"), perpetrated this stock manipulation through a variety of deceptive devices, artifices, and tactics that are the hallmarks of stock manipulation.

7. Plaintiff, in reliance on the continuing positive recommendations of ML with respect to the ML Stocks, retained them in his portfolio and recommended to his clients that they, too, hold such stocks, when, had he been advised of the true facts, would have sold them and advised his clients to sell them well before the ML Stocks dramatically declined in value.

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8. First, ML demanded that brokers in its various retail offices throughout the country sell the ML Stocks to public customers without regard to the propriety of these stocks as an investment for these customers. This was done to artificially create a market for the ML Stocks. ML withheld from its Brokers material information it knew about the stocks, including the fact of its artificial support of the price of such stocks.

9. ML regularly and systematically disseminated instructions to its brokers that they were required to identify and promote to customers of ML the ML Stocks, to whom such brokers would, in turn, recommend to their customers the purchase of these stocks. The company-wide demand for such purchases resulted from a systemic policy that brokers actively recommend and solicit purchases of these ML Stocks.

10. Second, ML systematically taught and encouraged its brokers to tell public customers not to sell the ML Stocks and utilized manipulative techniques to prevent such sales or otherwise make selling these stocks onerous. Again, ML never disclosed to its brokers the real basis for its recommendations to purchase the ML Stocks or to retain such stocks once purchased.

11. ML required its brokers to discourage and in some cases to refuse to allow customers to execute sell orders relating to ML Stocks.

12. Third, ML and certain of its agents, employees and affiliates opened brokerage accounts with ML for the purpose of engaging in the trading of ML Stocks.

13. Fourth, ML through its "research department" issued falsely favorable reports about ML Stocks without disclosing the manipulative scheme, or the exceptional relationships between these stocks and the investment banking arm of ML. These reports were distributed to ML brokers in their efforts to solicit purchases of these stocks. ML brokers were directed to rely upon these false reports and were further directed to not rely on any non-ML generated sources of information. In addition, these deceptive reports were disseminated to individuals not affiliated with ML in an effort to encourage widespread purchasing of these stocks and to artificially support the stocks prices.

14. In addition to the illegal sales efforts of ML, ML also artificially propped up the price of various ML Stocks by refusing to execute and otherwise actively discouraging the execution of orders to sell these stocks. These efforts improperly restrained investor selling, caused the supply of these stocks in the marketplace to be understated, caused the demand for these ML Stocks in the marketplace to be overstated, and, as a result, further caused the price of these stocks to be artificially inflated.

15. Plaintiff incorporates herein by reference all of the factual allegations of Eric R. Dinallo, Chief of the Investment Protection Bureau of the New York State Department of Law, also filed in the Supreme Court of the State of New York, County Of New York, a copy of which (without exhibits[1]) is attached hereto as *Exhibit B*.

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1. A copy of the exhibits to such affidavit will be provided to the Court and to counsel for ML upon request.

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16. ML's motive was clear: to enhance and support its competitive edge in its underwriting business by keeping the prices of stocks of companies for which it performed underwriting business at artificially elevated levels, all to ML's personal benefit and to the detriment of Plaintiff. As a result of ML's efforts, the stature of such companies was elevated, and those companies were better able to use their stock as currency in transactions and generally enjoyed enhanced reputations. ML would then use such stature to advertise for and attract further and additional investment banking business. ML would often pursue investment banking deals by touting the support its retail brokers could give to a stocks price thereby enriching the executives of ML's potential investment banking clients. Many of the false and misleading research recommendations on ML Stocks were also used to aid ML in its attempt to build its franchise in the internet and data services sector, where it theretofore had almost no market share or presence.

17. In the case of the ML Stocks, ML successfully propped up the price of these stocks and in exchange received numerous lucrative underwriting and investment banking engagements from such companies as well as other companies.

18. By propping up stocks that ML's "research department" recommended — purportedly on the basis of sound financial analysis — ML sought to establish its "research department" personnel as credible securities analysts in an effort to bolster an overall image of legitimacy.

Appendix D

19. Finally, by artificially inflating and/or artificially supporting the price of the ML Stocks, ML was able to generate larger investment banking fees for itself and higher volumes of investment banking fees, all to the detriment of Plaintiff and other Brokers and in violation of its fiduciary duties to Plaintiff and other Brokers.

JURISDICTION AND VENUE

20. The claims asserted herein arise under and pursuant to a breach of ML's fiduciary duty to Plaintiff and other Brokers and breach of the covenant of good faith and fair dealing between ML and its Brokers.

21. This Court has jurisdiction of this action pursuant to 28 U.S.C. § 1331 diversity jurisdiction. The amount in controversy exceeds $75,000.00.

22. Venue is properly laid in this District. Many of the acts and conduct complained of, including orchestration of a fum-wide manipulation of stocks by ML through its various branch brokerage offices around the world, emanated from and occurred in this district. Plaintiff resides in this district.

23. ML maintained a fully staffed brokerage office in Oklahoma City, Oklahoma at all relevant times, and conducted many of the acts complained of herein in this district.

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PARTIES

24. Plaintiff Shadi Dabit is a former ML broker who owned and held many of the ML Stocks during the Class Period, and has been damaged thereby. Plaintiff had numerous clients that purchased and held the ML Stocks on the basis of ML's recommendations, and thereafter terminated their relationship with Plaintiff upon learning of the true value of such stocks.

25. Defendant ML touts itself as one of the world's largest full service securities brokerage and investment banking firms, and maintains branch offices in locations throughout the world.

26. ML also touts itself as one of the world's leading financial management and advisory companies, with offices in 38 countries and total client assets of approximately S1.5 trillion. As an investment bank, ML has mushroomed to be a global underwriter of debt and equity securities and strategic advisor to governments, corporations and institutions and individuals worldwide. Through ML Investment Managers, ML is one of the world's largest managers of financial assets.

HISTORY OF THE PROBLEM

27. On June 14, 2001, the United States House of Representatives Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises (the "Subcommittee") began holding a hearing entitled "Analyzing the Analyst: Are Investors Getting Unbiased Research From Wall Street?" In his opening remarks, representative Paul E. Kanjorski, the ranking democratic member of the Subcommittee, stated:

> Unlike some other sources of investment advice, the vast majority of the general public has usually

considered the research prepared by Wall Street experts as reliable and valuable. With the burst of the high tech bubble, however, came rising skepticism among investors concerning the objectivity of some analysts over optimistic recommendations. Many in the media have also asserted that a variety of conflicts of interest may have gradually depreciated analysts' independence during the internet craze and effected the quality of their opinions. We have debated the issues surrounding analysts' independence for many years. After the deregulation of trading commissions in 1975, Wall Street firms began using investment banking as a means to compensate their research departments, and within the last few years the tying of analyst compensation to investment banking activities has become increasingly popular. As competition among brokerage firms for IPO's, mergers and acquisitions grew, so did the potential for large compensation packages for sale-side analysts. These pay practices, however, may have also effected analysts' independence. While some brokerage houses suggest that they have executed an impenetrable Chinese wall that divides analyst research from other firm functions like investment banking and trading, the truth, as we have learned from many recent news stories, is that they must initiate a proactive effort to rebuild their imaginary walls.

The release of some startling statistics has also called in to question the actual independence of

analyst. A report by First Call, for example, found that *less than 1% of 28,000 recommendations issued by brokerage analysts during the late 1999's and most of 2000 called for investors to sell stocks in their portfolios.* Within the very same time frame, the NASDAQ composite average fell dramatically. In hindsight, these recommendations appear dubious. Furthermore, First Call has determined that the ratio of buy-to-sell recommendations by brokerage analysts *rose from 6:1 in the early 1990's to 100:1 in 2000.* Many parties have consequently suggested that analysts may have become merely cheerleaders for the investment banking division in their brokerage houses. I agree. To me, it appears we may have obsequious analysts instead of objective analysts.

28. The erosion of analysts' objectivity that Rep. Kanjorski discussed was particularly manifest at ML, which employed several well-known analysts who had substantial influence on Wall Street.

29. Throughout the Class Period ML's ratings, reports, and recommendations regarding the ML Stocks were false and contained misleading statements, designed to artificially inflate and artificially support the price of the ML Stock. Rather than providing unbiased research and recommendations as publicly advertised and proclaimed, ML acted for its own self interest as an investment banker, participating in deal making and business generating activities in the hope of securing lucrative investment banking fees and substantial compensation for itself, at the expense of its brokers and customers.

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30. Plaintiff, while employed as a ML broker, was not aware of the conflicts of interest that lay at the heart of ML's research and analysis department, with the consequence that the securities he bought and held, individually and on behalf of his clients, which reflected the materially false and misleading reports in statements by ML, were artificially inflated and artificially supported throughout this period of time. Plaintiff, believing in the integrity of his employer and the ML Stocks' market prices as presented by ML, was damaged as a result of ML's unlawful conduct as described herein and saw his customers abandon him when the value of their portfolios evaporated.

HISTORY OF THE ANALYSTS

31. ML securities analysts who were employed by ML during the operative times reflected herein published two types of reports which were received by investors. Brokers for institutional investors received lengthy detailed reports while brokers for individuals received very short non-descriptive reports. Plaintiff and, in turn, his clients, relied on the reports and ratings which ML knew were not accurate and incorrect.

32. Historically, ML performed both investment banking and research analysts functions, but ML allegedly maintained a "Chinese" wall between the two functions to ensure that the analysts' research and recommendations remained "objective" and were not influenced by ML's interest in attracting and retaining investment banking business.

33. In recent years, however, the Chinese wall either crumbled or turned into rice paper, with research analysts

directly performing investment banking functions and receiving compensation based on their contributions to generating investment banking business, including underwriting initial public offerings and secondary offerings of equity securities, underwriting debt offerings and performing services in merger and acquisition transactions without disclosing material conflicts of interest to the investing public or ML's Retail Brokers.

34. During the Class Period ML made materially false and misleading statements designed to encourage Plaintiff and Plaintiff's clients to purchase ML Stocks. The recommendations were based not on objective analysis, but rather on ML's desire to attract and retain investment banking business for ML. ML's ratings, recommendations and positive comments regarding various stocks, including ML Stocks in which ML was a market maker during this period of time, were improperly influenced by their desire to increase their revenues and the undisclosed personal compensation of the analysts who were benefitting thereby.

35. The conflict of interest for ML's analysts remained undisclosed as they continued to inflate ratings and recommendations for various stocks, including ML Stocks, throughout late 1999 and early 2000. ML knew or should have known that the financial condition and future business prospects of the corporations behind these stocks did not support ML's positive comments and buy recommendations, but ML nevertheless continued to issue positive reports encouraging investors, including Plaintiff to purchase and/or hold the ML Stock.

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36. In some cases, ML simply refused to downgrade its stock recommendations because that would potentially impair ML's ability to generate additional investment banking business that ML wished to underwrite.

37. ML's efforts were designed to, and did, effect an artificial inflation of the price of ML Stocks, while simultaneously attracting and retaining the underlying corporations as ML investment banking clients.

38. After the market for internet and technology stocks collapsed in the first quarter of 2000, journalists, academics, and others began to expose the truth about the roles of analysts, including those at ML.

39. The conflicts of interest exhibited by ML analysts also began to draw the attention of various state and federal government authorities. ML did not timely disclose to Plaintiff that regulators were investigating ML's practices as described herein.

40. During the Class Period, ML continually promoted its stocks in the press, on television and the internet. This publicity campaign was intended to and did assure Plaintiff of ML's alleged integrity and expertise and reached not only investors who were brokerage customers of Plaintiff at ML, but also individual investors, not ML customers.

41. At the height of the internet boom in late 1999 and early 2000, ML analysts were virtually indistinguishable from their investment bankers. This material fact, however, was not disclosed in connection with ML's ratings, recommendations

and other statements regarding the stocks ML was pumping up. ML also withheld this fact from Plaintiff.

42. Unlike firms that did not do investment banking business, ML continued to keep or hold buy recommendations and continued to make highly complimentary comments about corporations with whom ML had done initial public offerings ("IPO"s) and whose stock prices were subsequently being pumped up or supported by ML in the secondary market.

43. When the price of these favored ML Stocks began to fall with the rest of the technology and internet market declines in the mid 2000's, ML still did not downgrade these stocks but instead continued to tout these ML Stocks ideas as excellent investments.

44. In some cases ML kept stock prices of ML Stocks from subsequently falling by continuing its campaign of false and misleading statements, including buy and strong buy recommendations.

45. ML's unlawful conduct allowed them to gain millions of dollars in investment banking fees during this period of time and allowed the analysts to receive millions of dollars in salaries and cash bonuses due to their false and misleading ratings, recommendations and pumped up statements.

46. During the time of the tech rise ML allowed analysts to personally buy and sell shares of stocks they followed.

47. ML, recognizing the problem it created, and as part of its cover up, announced on July 12, 2001, that it would

prohibit research analysts from buying stock in the companies they cover. ML did not, however, self disclose the corrupt system it had implemented and fostered prior to that date.

PLAINTIFF'S CLASS ACTION ALLEGATIONS

48. Plaintiff brings this action as a class action pursuant to Federal Rules of Civil Procedure 23(a) and 23(b)(3) on behalf of himself and on behalf of a class (the "Class") of persons who, while employed by ML as Retail Brokers, purchased or otherwise acquired, individually or on behalf of the Classes' clients, any of the ML Stocks during the period from December 1, 1999 through and including December 31, 2000 (the "Class Period"), and were damaged thereby. Excluded from the Class is the defendant herein; the directors and officers of ML; any corporation, firm, partnership, trust or other person affiliated with any of the foregoing; and the legal representatives, agents, heirs, successors-in-interest or assigns of any excluded person.

49. The members of the Class are so numerous that joinder of all members is impracticable. The precise number of Class members is unknown to Plaintiff at this time but Class members are believed to number in the thousands.

50. Plaintiff will fairly and adequately represent and protect the interests of the members of the Class. Plaintiff has retained competent counsel experienced in class action litigation to further ensure such protection and intend to prosecute this action vigorously.

51. Plaintiffs claims are typical of the claims of the other members of the Class because Plaintiff and all the Class

members' damages arise from and were caused by the same series of deceitful acts undertaken by or chargeable to ML. Plaintiff does not have interests antagonistic to, or in conflict with, the Class.

52. A Class Action is superior to other available methods for the fair and efficient adjudication of this controversy. As the damages suffered by individual class members may be relatively small, the expense and burden of individual litigation make it virtually impossible for most class members individually to seek redress for the wrongful conduct alleged. Plaintiff knows of no difficulty that will be encountered in the management of this litigation that would preclude its maintenance as a class action.

53. Common questions of law and fact exist as to all members of the Class and such questions predominate over any questions affecting solely individual members of the Class. Among the questions of law and fact common to the Class are:

(a) Whether the actions by ML constituted breach of fiduciary duty and breach of the duty of good faith and fair dealing;

(b) whether ML participated directly or indirectly in the concerted action or course of conduct complained of herein;

(c) whether ML artificially inflated or artificially supported recommended stocks through manipulative conduct as complained of herein; and

(d) the extent of injuries sustained by members of the Class and the appropriate measure of damages.

54. The names and addresses of class members, or their prior addresses are available from records maintained by ML. Notice can be provided to Class Members by a combination of published notice and first class mail using techniques and forms of notice similar to those customarily used in similar class actions.

CLAIMS FOR RELIEF

COUNT I

Breach of Fiduciary Duty

55. Plaintiff repeats and realleges each and every allegation contained above.

56. Defendant, directly and indirectly, engaged and participated in a continuous course of deceitful conduct to artificially raise and maintain the artificially inflated and artificially supported market price of the ML recommended stocks during the Class Period.

57. Defendant employed devices, schemes and artifices to defraud and engaged in acts, practices, and a course of conduct as alleged herein to deceive and misrepresent to Plaintiff and Plaintiff's customers the value of and demand for these stocks, which actions breached ML's fiduciary duty to its Retail Brokers.

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58. At the time of the course of conduct alleged above, Plaintiff and the other members of the Class were ignorant of the nature of ML's scheme. Plaintiff and the class members could not in the exercise of reasonable diligence have known the actual facts. Plaintiff and other members of the Class recommended these stocks to their customers and were induced to and did purchase these stocks at artificially inflated and supported prices. Had Plaintiff and other members of the Class known the truth, they would not have taken such action.

59. Defendant ML, with knowledge of, or in reckless disregard of, the conduct complained of herein, caused and permitted the actions which are alleged to have occurred.

60. By virtue of the foregoing, ML violated fiduciary duties to its Retail Brokers.

61. Plaintiff and other members of the Class have been damaged by defendants' violations as described in this Count and seek recovery for the damages caused thereby.

COUNT II

Breach of The Covenant of Good Faith and Fair Dealing

62. Plaintiff repeats and realleges the allegations set forth above as if set forth fully herein.

63. The wrongful acts alleged herein violated ML's requirement of good faith and fair dealing towards Plaintiff and the class members. ML failed to act in a manner

consistent with its representations to the class members or in a manner which a reasonable person would regard as fair and honest or in good faith.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff, on his own behalf and on behalf of the Class, prays for judgment as follows:

A. Declaring this action to be a class action properly maintained pursuant to Rule 23(a) and (b)(3) of the Federal Rules of Civil Procedure;

B. Awarding Plaintiff and the other members of the Class damages, including punitive damages, as provided by law;

C. Awarding Plaintiff and other members of the Class their costs and expenses of this litigation, including reasonable attorneys' fees, accountants' fees and experts' fees and other costs and disbursements; and

D. Awarding Plaintiff and other members of the Class such other and further relief as may be just and proper under the circumstances.

Signed this 26th day of April, 2002.

JURY TRIAL DEMANDED

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Respectfully Submitted,

s/ William B. Federman
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2800 First Oklahoma Tower
Oklahoma City, Ok 73102
Telephone: (405) 235-8318

[Exhibits intentionally omitted because they are set forth as Exhibits to Appendix F at pages 70a-120a.]

APPENDIX E — ORDER OF THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA DATED AND FILED OCTOBER 11, 2002

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA

Case No. CIV-02-564-F

SHADI DABIT, on behalf of himself and all others similarly situated,

Plaintiffs,

vs.

MERRILL LYNCH PIERCE FENNER & SMITH, INC., a corporation,

Defendant.

ORDER

Before the court is the defendant's Motion to Dismiss, filed July 18, 2002 (docket entry no. 26). The motion invokes only subdivision (6) of Rule 12(b), Fed.R.Civ.P. The plaintiff has responded and the defendant has filed a reply in support of the motion.

At the risk of oversimplification, plaintiff, as the proposed representative of a proposed class of similarly situated individuals (retail brokers employed by defendant during the proposed class period), asserts that, in violation of a common law duty of good faith and fair dealing and in

violation of a common law fiduciary duty, defendant wrongfully induced plaintiff and to purchase and hold, and to cause his clients to purchase and hold, securities for reasons which served defendant's proprietary interests and which were unrelated to the merits of the securities or the interests of the clients, with resultant reputational and other harm to plaintiff and the other class members.

Defendant asserts in its motion that plaintiff's class action claims are preempted by the Securities Litigation Uniform Standards Act of 1998 (SLUSA), 112 Stat. 3227 (codified in various places in 15 U.S.C.) and that they must be dismissed under the preemptive and preclusive language of SLUSA, 15 U.S.C. §§ 78bb(f)(1). Defendant further asserts that plaintiff's claims should be dismissed because they do not allege a cognizable legal theory under Oklahoma law.

Plaintiff, in response to the motion, argues that his claims are not preempted by SLUSA because his claims are predicated upon having been wrongfully induced to *hold*, rather than *purchase*, covered securities. Plaintiff also requests that "if the court is of the opinion that Dabit's claims are not sufficiently delineated in the Complaint to be beyond the reach of SLUSA, the court should grant Plaintiff leave to amend the Complaint to correct same." Plaintiff's response, at 10. Plaintiff requests, alternatively, that he be granted leave to plead federal securities claims if the court is of the opinion that it would not be possible for plaintiff to allege claims which would not be preempted by SLUSA. Id. Finally, plaintiff argues that, as a matter of Oklahoma law, he has stated claims for breach of fiduciary duty and breach of the implied covenant of good faith and fair dealing.

Appendix E

The court has concluded that the Complaint must be dismissed, with leave to amend. It is clear that, for some purposes, it will likely be necessary to differentiate between claims and damages based on wrongfully-induced purchases, on one hand, and claims and damages based on wrongfully-induced holding, on the other hand. However, the relevant allegations in the Complaint consist of a hopeless melange of purchase-related and holding-related assertions. They simply cannot be sorted out in any meaningful way. Conceptually, it is certainly conceivable that claims based on wrongfully-induced holding could be pleaded. In this respect, it should be noted that, as a matter of Oklahoma law, the court is not impressed with defendant's contention that Merrill Lynch's alleged misdeeds are not actionable at the instance of a retail broker who relied to his detriment upon the allegedly duplicitous research generated by Merrill Lynch. As was explained in *Roberson v. PaineWebber, Inc.*, 998 P.2d 193, 198 (Okla. App. 1999) (cert. denied 2000):

> A fiduciary relationship springs from an attitude of trust and confidence and is based on some form of agreement, either expressed or implied, from which it can be said the minds have been met to create a mutual obligation. [Citation omitted.] In determining whether a fiduciary relationship was established, several factors have been adopted to serve as guide for this fact-driven question. It includes not only all legal relationships, e.g., guardian and ward, attorney and client, but it extends to every possible case from which there is confidence reposed on one side and resulting domination and influence on the other. The

> relationship need not be legal as the relationship may develop because of moral, social, domestic or merely personal relations. The term "fiduciary relationship" is a very broad term and has been applied in circumstances where influence has been acquired and abused and where confidence has been reposed and betrayed. The origin of the confidence and the source of the influence are immaterial. The question is whether a relation in fact exists.

Cf., *Restatement (Second) of Agency*, §§ 434, 437, 470 (esp. Comment *c*, as to which intentional misconduct would present an *a fortiori* case), 472, 473. However, it falls to the plaintiff to allege viable claims which lend themselves to logical analysis. The question of whether a viable free-standing claim can be pleaded, and the related question of whether it will be feasible to fuse state law claims based on *holding* with federal claims based on *purchases* (if plaintiff elects to attempt to do so), will await another day.

The complaint is accordingly DISMISSED. Plaintiff is granted leave to file an amended complaint within ten days after the date of this order. In the amended complaint, plaintiff is at liberty to plead any combination of state and federal claims, in the alternative or otherwise, but state claims must be differentiated from federal claims, in terms of the substantive bases for liability and in terms of causation and damages.

DATED October 11, 2002.

s/ Stephen P. Friot
STEPHEN P. FRIOT
UNITED STATES DISTRICT JUDGE

APPENDIX F — FIRST AMENDED CLASS ACTION COMPLAINT WITH EXHIBITS DATED OCTOBER 21, 2002

UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA

Case No. CIV-02-564-F

SHADI DABIT,
on behalf of himself and all others similarly situated,

Plaintiff,

v.

MERRILL LYNCH PIERCE FENNER SMITH, INC.,
a corporation

Defendants.

FIRST AMENDED CLASS ACTION COMPLAINT

Plaintiff makes the following allegations upon information and belief, except as to allegations specifically pertaining to plaintiff and his counsel, based on the facts alleged below, predicated upon the investigation undertaken by plaintiff's counsel, Plaintiff believes that further substantial evidentiary support will exist for the allegations set forth below after a reasonable opportunity for discovery.

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NATURE OF THE ACTION

1. This is a class action brought by plaintiff on behalf of himself and all other former or current account executives ("Brokers") who, while employed by Defendant, Merrill Lynch Pierce Fenner & Smith, Inc. ("ML"), owned and continued to own one or more of the ML recommended securities identified in *Exhibit A*, attached hereto (the "ML Stocks"), or recommended such securities to their clients during the period from December 1, 1999 through December 31, 2000 (the "Class Period"), and who suffered damages as a result of owning and holding such ML Stocks during this time period, or who suffered damages as a consequence of the loss of clients due to ML's wrongful actions further described herein.

2. Plaintiff alleges that ML, after Plaintiffs purchase of the ML Stocks, individually or on behalf of clients of Plaintiff, failed to advise Plaintiff of the fact of the decreasing values of the ML Stocks, and misrepresented to Plaintiff that the ML Stocks were worthy of holding in Plaintiff's or Plaintiff's clients' portfolio, all in violation of ML's fiduciary duty to Plaintiffs and in violation of ML's covenant of good faith and fair dealing.

3. When the true value of the ML Stocks and individual portfolios too, became apparent and clients of Plaintiff terminated their relationship with Plaintiff, Plaintiff suffered damages in the form of lost commissions that would otherwise have been earned from future business with such clients.

4. Throughout the Class Period the price of the ML Stocks promoted by ML were artificially inflated as a result of the manipulative efforts of ML. As a result of the efforts of ML and its agents, employees and affiliates, ML was able to, and did, manipulate the price of the ML Stocks, causing these stocks to trade at artificially inflated prices.

5. Further, after regulatory authorities in the State of New York initiated investigations concerning ML's conduct in approximately June, 2001, and as pressure from those investigations increased, ML ceased manipulating the price of various stocks and, as a result, the market value of such stocks declined, leaving Plaintiff and clients of Plaintiff who held these stocks at manipulated inflated prices with substantial losses. ML failed to advise Plaintiff: of its breach of fiduciary duty; its false and artificial support of the ML stocks; the fact of the investigations and the certain subsequent decline in the ML Stocks' values once the investigations became known, thereby preventing Plaintiff from selling his personally held stocks at a minimal loss, and further preventing Plaintiff from advising his clients to similarly sell the ML Stocks in their individual portfolios.

6. ML, acting as a central nerve center in the manipulation of various stocks identified by the New York Attorney General ("NYAG"), perpetrated this stock manipulation through a variety of deceptive devices, artifices, and tactics that are the hallmarks of stock manipulation.

7. Plaintiff, in reliance on the continuing positive recommendations and support of ML with respect to the ML Stocks, retained them in his portfolio and recommended to

his clients that they too hold such stocks, when, had he been advised of the true facts, would have sold them or recommended that clients sell them well before the ML Stocks dramatically declined in value.

8. ML systematically taught and encouraged its Brokers to tell clients to own and hold the ML Stocks. ML never disclosed to its Brokers the real basis for its recommendations to hold such stocks.

9. ML and certain of its agents, employees and affiliates without advising Plaintiff traded against ML's published research recommendations, leaving the Brokers and their clients to provide support for the Company's stock prices.

10. ML caused the ML "research department" to issue falsely favorable reports about ML Stocks without disclosing the manipulative scheme, or the exceptional relationships between these stocks and the investment banking arm and officers of ML. These false reports were distributed to ML Brokers. ML Brokers were directed to rely upon these false reports and were further directed to not rely on any non-ML generated sources of information. In addition, these deceptive reports were disseminated to individuals not affiliated with ML in an effort to artificially support the stocks prices.

11. ML artificially propped up the price of various ML stocks by refusing to execute and otherwise actively discouraging the execution of orders to sell these stocks. These efforts improperly restrained investor selling, caused the supply of these stocks in the marketplace to be understated, caused the demand for the stocks in the

marketplace to be overstated and, as a result, further caused the price of these stocks to be artificially inflated and/or maintained.

12. Plaintiff incorporates herein by reference all of the factual allegations of Eric R. Dinallo, Chief of the Investment Protection Bureau of the New York State Department of Law, also filed in the Supreme Court of the State of New York, County Of New York, a copy of which (without exhibits[1]) is attached hereto as *Exhibit B*.

13. ML's motive was clear: to enhance and support its competitive edge in its underwriting business by keeping the prices of stocks of companies for which it performed underwriting business at artificially elevated levels, all to ML's personal benefit and to the detriment of Plaintiff and members of the class. As a result of ML's efforts, the stature of such companies was elevated, and those companies were better able to use their stock as currency in transactions and generally enjoyed enhanced reputations. ML would then use such stature to advertise for and attract further and additional investment banking business. ML would often pursue investment banking deals by touting the support its retail brokers could give to a stock's price thereby enriching the executives of ML's potential investment banking clients. Many of the false and misleading "research" reports on ML Stocks were also used to aid ML in its attempt to build its franchise in the internet and data services sector, where it previously had almost no market share or presence.

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1. A copy of the exhibits to such affidavit is a public record and can be provided to the Court and to counsel for ML upon request.

14. In the case of the ML Stocks, ML successfully propped up the price of these stocks and in exchange received numerous lucrative underwriting and investment banking engagements from such companies as well as other companies.

15. By propping up stocks that ML's "research department" recommended —purportedly on the basis of sound financial analysis — ML sought to establish its "research department" personnel as credible securities analysts in an effort to bolster an overall image of legitimacy.

16. Finally, by artificially inflating and/or artificially supporting the price of the ML Stocks, ML was able to generate larger and higher volumes of investment banking fees to the detriment of Plaintiff and members of the class.

JURISDICTION AND VENUE

17. The claims asserted herein arise under and pursuant to a breach of ML's fiduciary duty to Plaintiff and breach of the covenant of good faith and fair dealing between ML and its Brokers.

18. This Court has jurisdiction of this action pursuant to 28 U.S.C. § 1331 (diversity jurisdiction). The amount in controversy exceeds $75,000.00.

19. Venue is properly laid in this District. Many of the acts and conduct complained of, including orchestration of a firm-wide manipulation of stocks by ML through its various branch brokerage offices around the world, emanated from and occurred in this district. Plaintiff resides in this district.

20. ML maintained a fully staffed brokerage office in Oklahoma City, Oklahoma at all relevant times, and conducted many of the acts complained of herein in this district.

PARTIES

21. Plaintiff Shadi Dabit ("Dabit"), as set forth in the accompanying certification, is a former ML Broker who owned and held many of the ML Stocks during the Class Period, and has been damaged thereby.

22. Defendant ML touts itself as one of the largest full service securities brokerage and investment banking firms, and maintains branch offices in locations throughout the world.

23. ML also touts itself as one of the world's leading financial management and advisory companies, with offices in 38 countries and total client assets of approximately $1.5 trillion. As an investment bank, ML has mushroomed to be a global underwriter of debt and equity securities and strategic advisor to governments, corporations and institutions and individuals worldwide. Through ML Investment Managers, ML is one of the world's largest managers of financial assets.

HISTORY OF THE PROBLEM

24. On June 14, 2001, the United States House of Representatives Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises (the "Subcommittee") began holding a hearing entitled "Analyzing the Analyst: Are

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Investors Getting Unbiased Research From Wall Street?" In his opening remarks, Representative Paul E. Kanjorski, the ranking democratic member of the Subcommittee, stated:

> Unlike some other sources of investment advice, the vast majority of the general public has usually considered the research prepared by Wall Street experts as reliable and valuable. With the burst of the high tech bubble, however, came rising skepticism among investors concerning the objectivity of some analysts over optimistic recommendations. Many in the media have also asserted that a variety of conflicts of interest may have gradually depreciated analysts' independence during the internet craze and affected the quality of their opinions. We have debated the issues surrounding analysts' independence for many years. After the deregulation of trading commissions in 1975, Wall Street firms began using investment banking as a means to compensate their research departments, and within the last few years the tying of analyst compensation to investment banking activities has become increasingly popular. As competition among brokerage firms for IPO's, mergers and acquisitions grew, so did the potential for large compensation packages for sale-side analysts. These pay practices, however, may have also effected analysts' independence. While some brokerage houses suggest that they have executed an impenetrable Chinese wall that divides analyst research from other firm functions like investment

banking and trading, the truth, as we have learned from many recent news stories, is that they must initiate a proactive effort to rebuild their imaginary walls.

The release of some startling statistics has also called in to question the actual independence of analyst. A report by First Call, for example, found that less than 1% of 28,000 recommendations issued by brokerage analysts during the late 1999's and most of 2000 called for investors to sell stocks in their portfolios. Within the very same time frame, the NASDAQ composite average fell dramatically. In hindsight, these recommendations appear dubious. Furthermore, First Call has determined that the ratio of buy-to-sell recommendations by brokerage analysts rose from 6:1 in the early 1990's to 100:1 in 2000. Many parties have consequently suggested that analysts may have become merely cheerleaders for the investment banking division in their brokerage houses. I agree. To me, it appears we may have obsequious analysts instead of objective analysts.

25. The erosion of analysts' objectivity that Rep. Kanjorski discussed was particularly manifest at ML, which employed several well-known analysts who had substantial influence on Wall Street,

26. Throughout the Class Period ML's ratings, reports, and recommendations regarding the ML Stocks were false and contained misleading statements, designed to artificially

inflate and artificially support the price of the ML Stock. Rather than providing unbiased research and recommendations as publicly advertised and proclaimed, ML acted for its own self interest as an investment banker, participating in deal making and business generating activities in the hope of seeming lucrative investment banking fees and substantial compensation for itself, at the expense of its brokers and customers.

27. Dabit, while employed as a ML Broker, was not aware of the conflicts of interest that lay at the heart of ML's research and analysis department. As a consequence, Dabit held securities and recommended that his clients hold securities in reliance upon the materially false and misleading statements made by ML. Plaintiff, believing in the honesty and integrity of his employer and the ML Stocks' market prices as presented by ML, was damaged as a result of ML's unlawful conduct as described herein and saw his customers abandon him when the value of their portfolios evaporated.

BACKGROUND AND HISTORY OF THE ANALYSTS' PROBLEM

28. ML securities analysts who were employed by ML during the operative times reflected herein published two types of reports which were received by investors. Brokers for institutional investors received lengthy detailed reports while brokers for individuals received very short non-descriptive reports. Plaintiff and, in turn, his clients, relied on the reports and ratings which ML knew were not accurate and not correct.

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29. Historically, ML performed both investment banking and research analysts' functions, but ML allegedly maintained a "Chinese" wall between the two functions to ensure that the analysts' research and recommendations remained "objective" and were not influenced by ML's interest in attracting and retaining investment banking business.

30. In recent years, however, the Chinese wall either crumbled or turned into rice paper, with research analysts directly performing investment banking functions and receiving compensation based on their contributions to generating investment banking business, including underwriting initial public offerings and secondary offerings of equity securities, underwriting debt offerings and performing services in merger and acquisition transactions without disclosing material conflicts of interest to the investing public or ML's Retail Brokers.

31. During 1999 and 2000, ML made materially false and misleading statements designed to encourage Plaintiff and Plaintiff's clients to continue to hold the ML Stocks. The recommendations were based not on objective analysis, but rather on ML's desire to attract and retain investment banking business for ML and to profit ML at the expense of the Brokers and their clients. ML's ratings, recommendations and positive comments regarding various stocks, including ML Stocks in which ML was a market maker during this period of time, were improperly influenced by their desire to increase their revenues and profits and the undisclosed personal compensation of the analysts who were benefiting thereby.

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32. The conflicts of interest for ML's analysts remained undisclosed as they continued to inflate ratings and recommendations for various stocks, including ML Stocks, throughout late 1999 and early 2000. ML knew that the financial condition and future business prospects of the corporations behind these stocks did not support ML's positive comments and buy recommendations, but ML nevertheless continued to issue positive reports encouraging investors, including Plaintiff, to hold the ML Stocks.

33. In some cases, ML simply refused to downgrade its stock recommendations because that would potentially impair ML's ability to generate additional investment banking business that ML wished to underwrite. In some cases, ML officers, affiliates and agents held ML recommended stocks because a downgrade by a ML analyst would materially adversely affect the ML stocks value.

34. ML's efforts were designed to, and did, effect an artificial inflation and artificial price of ML Stocks, while simultaneously attracting and retaining the underlying and new corporations as ML investment banking clients.

35. After the market for internet and technology stocks collapsed in the first quarter of 2000, journalists, academics, and others began to expose the truth about the roles of analysts, including those at ML.

36. The conflicts of interest exhibited by ML analysts also began to draw the attention of various state and federal government authorities. ML did not timely disclose to Plaintiff that regulators were investigating ML's practices as described herein.

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37. During the Class Period, ML continually promoted the ML Stocks in the press, on television and the internet. This publicity campaign was intended to and did assure Plaintiff of ML's alleged integrity and expertise and reached not only investors who were brokerage customers of Plaintiff at ML, but also individual investors, not ML customers.

38. At the height of the internet boom in late 1999 and early 2000, ML analysts were virtually indistinguishable from their investment bankers. This material fact, however, was never disclosed in connection with ML's ratings, recommendations and other statements regarding the stocks ML was pumping up. ML also withheld this fact from Plaintiff.

39. Unlike firms that did not do investment banking business, ML continued to keep or hold buy recommendations and continued to make highly complimentary comments about corporations with whom ML had conducted initial public offerings ("IPO's") and whose stock prices were subsequently being pumped up or supported by ML in the secondary market.

40. When the price of these favored ML Stocks began to fall in the mid 2000's, ML was still not downgrading the stocks but instead continued to tout these ML Stocks as excellent investments for Plaintiff and his clients to continue to hold. Sometimes, at the same time as it was touting it Brokers and clients to hold the ML Stocks, ML and its agents and affiliates were selling their positions.

41. In some cases ML kept stock prices of ML Stocks from subsequently falling by continuing its campaign of false and misleading statements, including maintaining and/or reiterating buy and strong buy recommendations.

42. ML's unlawful conduct allowed it to earn millions of dollars in investment banking fees during this period of time and allowed its analysts to receive millions of dollars in salaries and cash bonuses due to their false and misleading ratings, recommendations and pumped up statements.

43. During the time of the technology rise, ML allowed analysts to personally buy and sell shares of stocks they followed, without ever disclosing such sales to Plaintiff.

44. ML, recognizing the problem it created, and as part of its cover up, finally announced on July 12, 2001, that it would prohibit research analysts from buying stock in the companies they cover. ML did not, however, self disclose the corrupt system it had implemented and fostered prior to that date.

PLAINTIFF'S CLASS ACTION ALLEGATIONS

45. Plaintiff brings this action as a class action pursuant to Federal Rules of Civil Procedure 23(a) and 23(b)(3) on behalf of himself and on behalf of a class (the "Class") of persons who, while employed by ML as Retail Brokers, held individually or on behalf of the Classes' clients, any of the ML Stocks during the period from December 1, 1999 through and including December 31, 2000 (the "Class Period"), and were damaged thereby. Excluded from the Class is the

defendant herein; the directors and officers of ML; any corporation, firm, partnership, trust or other person affiliated with any of the foregoing; and the legal representatives, agents, heirs, successors-in-interest or assigns of any excluded person.

46. The members of the Class are so numerous that joinder of all members is impracticable. The precise number of Class members is unknown to Plaintiff at this time but Class members are believed to number in the thousands.

47. Plaintiff will fairly and adequately represent and protect the interests of the members of the Class. Plaintiff has retained competent counsel experienced in class action litigation to further ensure such protection and intend to prosecute this action vigorously.

48. Plaintiff's claims are typical of the claims of the other members of the Class because Plaintiff and all the Class members' damages arise from and were caused by the same series of deceitful acts undertaken by or chargeable to ML. Plaintiff does not have interests antagonistic to, or in conflict with, the Class.

49. A Class Action is superior to other available methods for the fair and efficient adjudication of this controversy. As the damages suffered by individual class members may be relatively small, the expense and burden of individual litigation may make it virtually impossible for most class members individually to seek redress for the wrongful conduct alleged. Plaintiff knows of no difficulty that will be encountered in the management of this litigation that would preclude its maintenance as a class action.

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50. Common questions of law and fact exist as to all members of the Class and such questions predominate over any questions affecting solely individual members of the Class. Among the questions of law and fact common to the Class are:

(a) Whether the actions by ML constituted breach of fiduciary duty and breach of the duty of good faith and fair dealing;

(b) whether ML participated directly or indirectly in the concerted action or course of conduct complained of herein;

(c) whether ML artificially inflated or artificially supported recommended stocks through manipulative conduct as complained of herein; and

(d) the extent of injuries sustained by members of the Class and the appropriate measure of damages.

51. The names and addresses of class members, or their prior addresses are available from records maintained by ML. Notice can be provided to Class Members by a combination of published notice and first class mail using techniques and forms of notice similar to those customarily used in similar class actions.

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CLAIMS FOR RELIEF

COUNT I

Breach of Fiduciary Duty

1. Plaintiff repeats and realleges each and every allegation contained above.

2. A fiduciary relationship existed between ML and Plaintiff and all members of the class because a special competence and confidence was placed in ML who, in equity and good conscience, was bound to act in good faith and with due regard for the interests of Plaintiff and all members of the class.

3. A confidential relationship arose between Ml and Plaintiff and all members of the class by reason of the professional and business relations between those parties as set forth hereinabove.

4. ML breached its fiduciary duties to Plaintiff and all members of the class in the manner described hereinabove.

5. Plaintiff and other members of the Class have been damaged by defendant's violations as described in this Count and seek recovery for the damages caused thereby.

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COUNT II

Breach of The Covenant of Good Faith and Fair Dealing

6. Plaintiff repeats and realleges the allegations set forth above as if set forth fully herein.

7. The wrongful acts alleged herein violated ML's requirement of good faith and fair dealing towards Plaintiff and the class members. ML failed to act in a manner consistent with its representations to the class members or in a manner which a reasonable person would regard as fair and honest or in good faith.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff, on his own behalf and on behalf of the Class, prays for judgment as follows:

A. Declaring this action to be a class action properly maintained pursuant to Rule 23(a) and (b)(3) of the Federal Rules of Civil Procedure;

B. Awarding Plaintiff and the other members of the Class damages, including punitive damages, as provided by law;

C. Awarding Plaintiff and other members of the Class their costs and expenses of this litigation, including reasonable attorneys' fees, accountants' fees and experts' fees and other costs and disbursements; and

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D. Awarding Plaintiff and other members of the Class such other and further relief as may be, just and proper under the circumstances.

Signed this 21st day of October, 2002.

JURY TRIAL DEMANDED

Respectfully Submitted,

s/ _____
William B. Federman, OBA #2853
Federman & Sherwood
120 N. Robinson, Suite 2720
Oklahoma City, OK 73102
Telephone: (405) 235-1560
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-and-

Clell I. Cunningham, OBA#2093
Dunn, Swan & Cunningham
2800 First Oklahoma Tower
Oklahoma City, OK 73102
Telephone: (405) 235-8318

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EXHIBIT A

Company Name	Symbol	Investment Banking Relationship
Aether	***AETH***	***YES***
Ariba	***ARBA***	***YES***
Applied Micro Circuits	***AMCC***	***NO***
Digital Island	***ISLD***	***YES***
Commerce One	***CMRC***	***NO***
Brocade	***BRCD***	***YES***
Broadcom	***BRCM***	***YES***
Barnesandnoble.com	BNBN	YES
CMGI, Inc.	***CMGI***	***NO***
Corio	CRIO	YES
Extreme Networks	EXTR	YES
Exfo Electro-Optical Engineering	EXFO	YES
Global Crossing	GBLXE*	YES
Internet Capital Group	***ICGE***	***YES***
DrKoop.com	KOOP	YES
EToys, Inc	ETYSQ*	YES
Exodus	***EXDS***	***YES***
Globix	***GBIX***	***YES***
Finisar	FNSR	YES
Infospace	INSP	YES
Exfo Electro-Optical Engineering	EXFO	YES
Vitria	***VITR***	***YES***
Doubleclick	***DCLK***	***YES***
Inktomi	***INKT***	***YES***
PMC Sierra	***PMCS***	***NO***

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Company Name	Symbol	Investment Banking Relationship (Cont'd)
Verisign	***VRSN***	***NO***
Akamai Technology	AKAM	YES
Foundry	FDRY	YES
McData	MCDT	YES
Microstrategy	***MSTR***	***YES***
Nextlink Communications	XOXO*	YES
Inrange Technology	INRG	YES
Yahoo!	***YHOO***	***NO***
Amazon.com	***AMZN***	***NO***
Pets.com	*	YES
Priceline.com	PCLN	YES
RealNetworks (Progressive Networks)	***RNWK***	***YES***
TheStreet.com	TSCM	YES
USN Communications	***USNC***	***YES***
Vitria Technology Inc.	***VITR***	***YES***
Webvan Group Inc.	WBVN	YES
JDS Uniphase	***JDSU***	***NO***
I2 Technologies	ITWO	NO
SDLI	***SDLI***	***YES***
Starmedia	STRM	YES
Sycamore	***SCMR***	***YES***
Juniper	***JNPR***	***NO***
Cacheflow Inc.	CFLO	NO

* Indicates company is now ***bankrupt*** and/or has been ***de-listed.***

Companies in bold and italics indicate Shadi Dabit owned company in his own account.

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EXHIBIT B

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

Index No.

IN THE MATTER OF

An Inquiry by ELIOT SPITZER,
Attorney General of the State of New York,

Petitioner,

Pursuant to Article 23-A of the General Business Law of the State of New York with regard to the acts and practices of

Merrill Lynch & Co., Inc., Henry Blodget, Justin Baldauf, Kirsten Campbell, Virginia Syer Genereux, Sofia Ghachem, Thomas Mazzuoco, Edward McCabe and Deepak Raj,

Respondents,

In the offer, sale, issuance, promotion, advertisement, exchange, marketing, distribution and transfer of, or investment advice for, securities in and from the State of New York.

AFFIDAVIT IN SUPPORT OF APPLICATION FOR AN ORDER PURSUANT TO GENERAL BUSINESS LAW SECTION 354

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County of New York)
ss:
State of New York)

Eric R. Dinallo, being duly sworn, deposes and says:

I am the Chief of the Investment Protection Bureau of the New York State Department of Law and am of counsel to Eliot Spitzer, Attorney General of the State of New York. I am familiar with the facts and circumstances of the above-captioned investigation that give rise to the within application. The following statements are made upon information and belief based upon an examination of records and documents in the possession of the New York State Department of Law and testimony taken before the Attorney General's Office. On behalf of Attorney General Eliot Spitzer, I submit this affidavit, together with exhibits, in support of the Attorney General's *ex parte* application for the attached order pursuant to Section 354 of the General Business Law ("GBL").

In June 2001, the Office of the Attorney General commenced an investigation pursuant to GBL Article 23-A (the "Martin Act") into stock recommendations issued by research analysts. The investigation includes recommendations on all stocks covered by the internet research analysts at Merrill Lynch and, very recently, has expanded to include recommendations made by analysts at several additional financial institutions.

The Office of the Attorney General has to date reviewed over 30,000 documents, comprising over 100,000 pages,

including thousands of e-mails. It has examined close to twenty witnesses under oath, and has consulted with other witnesses, their lawyers, and experts. While Merrill Lynch has been cooperative in producing evidence, some of the witnesses examined have displayed an implausible lack of recollection of key conversations and documents, even when they authored or received such document and it was placed before them. This lack of recollection often related to events and documents that one would be unlikely to forget. The credibility of these witnesses is consequently suspect. Thus, further testimony is sought under judicial supervision and with public scrutiny.

The Attorney General, having determined to commence an action pursuant to GBL Article 23-A, seeks this relief pursuant to GBL §354, which provides that the Attorney General may apply for an *ex parte* order to obtain respondents' testimony, books and records when he believes the same to be "material and necessary" to his investigation of their activities in the offer, sale, and purchase of securities, and investment advice for such securities, within and from the State of New York. GBL §354 further provides that the Supreme Court shall grant such application as a matter of course, along with a preliminary injunction or stay, as is "proper and expedient."

The public testimony, books and records of respondents in this proceeding are material and necessary to the investigation being conducted by the Attorney General. Further, as detailed below, information has come to the attention of the Attorney General that establishes the need for immediate equitable intervention by this Court to prevent

further fraud, to protect the rights of the investing public, and to educate it about the enclosed material pending completion of the Attorney General's investigation into Merrill Lynch and other financial institutions.

I. INTRODUCTION

Since late 1999, the internet research analysts (the "internet group") at Merrill Lynch have published on a regular basis ratings for internet stocks that were misleading because: (1) the ratings in many cases did not reflect the analysts' true opinions of the companies; (2) as a matter of undisclosed, internal policy, no "reduce" or "sell" recommendations were issued, thereby converting a published five-point rating scale into a *de facto* three-point system; and (3) Merrill Lynch failed to disclose to the public that Merrill Lynch's ratings were tarnished by an undisclosed conflict of interest: the research analysts were acting as quasi-investment bankers for the companies at issue, often initiating, continuing, and/or manipulating research coverage for the purpose of attracting and keeping investment banking clients, thereby producing misleading ratings that were neither objective nor independent, as they purported to be.

Behind these ratings was a serious breakdown of the separation between the Merrill Lynch banking and research departments, a separation that was critical to the integrity of the recommendations issued to the public by Merrill Lynch. Though Merrill Lynch's stated policies reflect an understanding that this separation is critical, the evidence reveals that at least with respect to the internet group, there was insufficient divide between research and banking.

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Our investigation to date reveals that the compensation system for internet analysts was a significant factor contributing to the breakdown between the internet group and investment banking departments. Research analysts knew that the investment banking business they generated or participated in would impact their compensation, and management encouraged them to produce investment banking business. Analysts curried favor with potential or actual investment banking clients by giving them special treatment. At times, officers of clients or prospective clients were allowed to redraft their own coverage, write quotations in which the analysts would tout their companies, and indicate which ratings would be acceptable to them.

The pressures put on the Merrill Lynch internet group to appease both investment bankers and clients led the group to ignore the bottom two categories of the five-point rating system ('reduce" and "sell") and to use only the remaining rating ("buy", "accumulate" and "neutral"). The absence of clear guidance from Merrill Lynch management on how to resolve the conflicts created by these pressures led respondent Henry Blodget, the head of the internet group, in a moment of candor, to threaten to "*start* calling the stocks (stocks, not companies) . . . like we see them, no matter what the ancillary business consequences are." (ML 68401) (emphasis added).[1]

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1. Submitted herewith is a volume of exhibits reflecting the following categories: "ML" refers to documents produced to the Attorney General's Office by Merrill Lynch; "OV" refers to documents produced by Overture Services, Inc.; "KC" refers to documents produced by Kirsten Campbell. "Tr." refers to transcript of testimony taken by the Attorney General's Office; "Exhibit" refers to documents introduced at testinony taken by the Attorney General's Office.

Based upon the foregoing and as explained below, the Attorney General seeks relief as described in the annexed proposed order.

II. PARTIES

The petitioner, Eliot Spitzer, is Attorney General of the State of New York. Pursuant to Article 23-A of the General Business Law, the Attorney General oversees the offer, sale, issuance, promotion, advertisement, exchange, marketing, distribution and transfer of, or investment advice for, securities within and from the State of New York, and has authority to seek judicial intervention when fraudulent activities have occurred or are about to occur. The Attorney General's principal office for oversight of the securities industry in New York State is located in New York County.

Respondent Merrill Lynch & Co. Inc. ("Merrill Lynch") is an international investment firm that provides investment banking services to businesses, engages in retail and institutional sales to its customers, and publishes research reports and ratings on stocks. Merrill Lynch's corporate headquarters are located in New York City.

Respondent Henry Blodget ("Blodget") was, until his departure from Merrill Lynch in December 2001, a managing director and head of the Internet Research group in New York City. Mr. Blodget reported to respondent Deepak Raj and Andrew Melnick.

Respondent Justin Baldauf ("Baldauf") is an analyst in the Internet Research group at Merrill Lynch in New York

City. Mr. Baldauf reported to respondent Blodget, and became head of the Internet Research group upon Mr. Blodget's departure from Merrill Lynch.

Respondent Kirsten Campbell ("Campbell") was, until her departure from Merrill Lynch in April 2001, a vice-president and analyst in the Internet Research group in New York City. Ms. Campbell reported to respondent Blodget.

Respondent Virginia Syer Genereux ("Syer") is a research analyst at Merrill Lynch in New York City. Ms. Syer reported to respondent Blodget.

Respondent Sofia Ghachem was an analyst in the Internet Research group at Merrill Lynch in New York City. Ms. Ghachem reported to respondent Blodget.

Respondent Thomas Mazzucco ("Mazzucco") is a managing director of Merrill Lynch's Investment Banking Technology group in Palo Alto, California.

Respondent Edward McCabe ("McCabe") was, until his departure from Merrill Lynch in December 2001, a first vice president and a senior analyst in the Internet Research group in New York City. Mr. McCabe reported to respondent Blodget.

Respondent Deepak Raj ("Raj") is head of Global Equity Research at Merrill Lynch in New York City.

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III. STATUTORY FRAMEWORK

Article 23-A of the General Business Law ("GBL") of the State of New York, commonly referred to as the "Martin Act," and the regulations issued pursuant thereto regulate the offer and sale of securities within and from the State of New York and authorize the Attorney General to investigate the conduct of persons and entities engaged in, *inter alia*, the issuance, exchange, purchase, sale, promotion, negotiation, advertisement, investment advice or distribution within or from the State of New York of any securities.

The Martin Act proscribes a wide array of practices in connection with the sale of securities. It prohibits and makes illegal any fraud, misrepresentation, deception, concealment, promise or representation that is beyond reasonable expectation while engaged in the issuance, distribution, investment advice, sale or purchase of securities within and from the State of New York. The statutory scheme also prohibits and makes illegal any artifice, device or scheme to obtain money by any means prohibited by General Business Law §352-c. Unlike the federal securities laws, no purchase or sale of stock is required, nor are intent, reliance, or damages required elements of a violation.

GBL Section 352 (1) defines fraud and fraudulent practices as including, *inter alia*, any device, scheme or artifice to defraud or obtain money by means of any false pretense, representation or promise, fictitious or pretended purchase or sale, and any concealment, suppression, fraud, false pretense or false promise in connection with the sale of securities or offering of investment advice. It also provides,

inter alia, that violation of any section of GBL Article 23-A is a fraudulent practice, and authorizes the Attorney General to investigate allegations of fraud.

When, based upon a preliminary investigation, the Attorney General determines to commence an action pursuant to Article 23-A, he may seek an *ex parte* application from the Supreme Court, pursuant to GBL §354, for an order directing the persons and entities mentioned in the application to appear and answer questions and to produce documents that the Attorney General believes to be material and necessary. In addition, the Attorney General may include with such application a request for a preliminary injunction or stay as maybe "proper and expedient." At the conclusion of the investigation, the Attorney General is empowered, under GBL §353, to seek an injunction permanently enjoining an individual or entity from directly or indirectly engaging in the issue, sale or offer of, or investment advice for, securities within or from the State of New York, as well as restitution, and/or, under GBL §352-c. to file criminal charges against such individuals or entity.

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IV. FACTS

A. *The Internet Group's Stock Ratings Were Misleading*

1. The Merrill Lynch Rating System: Theory Versus Reality

Until June 15, 2001, Merrill Lynch had a five-category stock rating system:

1 Buy (20% or more price growth expected)
2 Accumulate (10% to 20% price growth expected)
3 Neutral (10% price growth to 10% price drop expected of price)
4 Reduce (10% to 20% price drop expected)
5 Sell (20% or more price drop expected)

(ML 02084-85).

Each covered stock was rated for both the intermediate-term (through the next twelve months) and long-term (beyond twelve months), and assigned an investment risk ranging from "A" (least risky) through "D" (most risky).[2] The ratings assigned to covered companies were represented to the investing public to be independent, objective and on the merits:

Objectivity of Opinions. Opinions expressed by Analysts must be objective. Any indication that a

2. All of the stocks discussed herein were assigned a "D" rating by the Merrill Lynch Internet group.

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> Research opinion is less than totally objective, or that it may have been influenced by a business relationship of the Firm, could seriously damage the Firm's reputation and lead to potential legal liability.

(ML 02063; *see also* ML 85893). Our investigation indicates that this was not the case with respect to ratings published by the Internet group.

Although Merrill Lynch's published rating system provided for 4s (reduce) and 5s (sell), the internet group never used 4s or 5s. The list of covered internet stocks for the second quarter of 2000, for instance, lists 24 stocks, none of which was rated less favorably than a 2. (ML 03747). From the spring of 1999 to the fall of 2001, Merrill Lynch never published a single reduce or sell rating on any stock covered by the Internet group. In their sworn testimony, both Blodget and his subordinate, respondent Kirsten Campbell, confirmed that the group never rated a stock 4 or 5. (Blodget Tr. at 115-19; Campbell Tr. at 36). Thus, although represented to be a five-point system, internally it became a three-point system. In lieu of assigning reduce or sell recommendations to stocks they no longer favored, the internet group instead merely quietly stopped covering the stock, without any announcement or meaningful explanation to the retail public. (ML 87610).

Thus, as previously covered stocks such as Pets.com, Mypoints.com. Quokka Sports, Webvan, iVillage, Buy.com. 24/7 Media, E-Toys, Internet Capital Group, and InfoSpace plummeted, sometimes all the way to zero, retail customers

and the investing public were never advised to sell. (ML 51690, ML 51833, ML 51997, ML 52195, ML 52516, ML 53160, ML 53161, ML 53162, ML 53181, ML 53507, ML 53612 and ML 53760; *see also* ML 87610). The reason for this failure is at least in part the substantial unrevealed conflict of interest discussed below.

2. The Ratings Assigned to Stocks Did Not Comport With Their Definitions

Although perhaps comforting to investment banking clients (who could be assured their stocks would never get a reduce or sell rating because "we don't cover anything below a 3" (OV 00276)), the de facto three-point system not surprisingly wreaked havoc amongst the various constituencies called upon to interpret and utilize the ratings, especially the retail public. While sophisticated institutional investors and equities traders may have recognized the de facto three-point scale, *see* (ML 55256-58) ("3-1 is a major red flag - short"), or may have specifically been told by the Internet group that, despite a stock's 3-1 rating there was nothing "interesting" about a company "except the [investment] banking fees" (ML 03806), the public and retail investors did not have such insight.

Thus, the public was unaware that while the Internet group was contemplating a 3 (neutral) rating on selected stocks, internally they were saying amongst themselves that the stock was "going a lot lower," (ML 09045), that the company was "crap," (ML 51453, 37899), or a "dog" (ML 37700). Nor was the public told that while the Internet group was contemplating a 2 (accumulate) rating on a variety of

stocks, internally — and to selected institutional investors — the analysts were saying that there was "(no) reason to buy more of" the stock and its business was "falling apart," (ML 74038), "[n]o reason to own" the stock, (ML 09045), or that the group expected the stock to be "flat" over the next six months without "any real catalysts [for change]" (ML 37956). The public also was not told that the group internally disparaged other stocks rated 2 as a "piece of shit," (ML 60903, 64372), and "such a piece of crap." (ML 51453).

The electronic communications of the Internet group feature many such exchanges. For example, on August 30, 1999, the group initiated coverage on the stock of Internet Capital Group (ICGE), an investment banking client, with a 2-1 rating. The stock closed on October 4, 2000 at $15.69, down from a high of $212 on December 22, 1999. On October 5, 2000 with the stock at $12.38, in an e-mail exchange with another senior analyst, Blodget predicted the stock was, "going to 5." (ML 63900). The next day he wrote in an e-mail: "No helpful news to relate [regarding ICGE], I'm afraid. This has been a disaster . . . there really is no floor to the stock." (ML 63901). But even with these prognostications, the public rating remained 2-1 and, when eventually downgraded on November 9, 2000, was changed only to a 2-2. The result was a continued recommendation to the investing public to purchase a stock about which the head of the Internet group was obviously exceptionally and accurately pessimistic, and for which he anticipated a drop of an additional 60 percent. (ML 63900-01; ML 64077; ML 53507). Despite this pessimistic outlook, ICGE was on Merrill Lynch's list of the top ten technology stocks ("Top Ten Tech" list), as late as September 12, 2000. (ML 62490-01).

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Under this regime, even a 1-1, Merrill Lynch's highest investment rating, could not be trusted. In one example, while a company's stock price was $96.50, the analysts, while reviewing a research note reiterating the 1-1 rating, wrote of the stock's prospects: "could go very low," "could hit $50 or $60 I think." (ML 63652).

Merrill Lynch maintained a list of its highest recommended stocks, selected from all of the stocks Merrill Lynch covered — not just internet stocks. To be selected for this list (the "Favored 15"), to which retail brokers and the public had access, a stock had to have a 1-1 rating. (ML 09639). InfoSpace was on the "Favored 15" List from at least August 2000 until December 5, 2000, even though Blodget had acknowledged as early as July 2000 that the stock was a "powder keg" and that "many institutions" had raised "bad smell comments" about it, and in October had referred to it as a "piece of junk." (ML 06413-14, ML06578) Oddly enough, Blodget was unaware that the stock he had been covering for months carried the imprimatur of the "Favored 15." (ML 61728, ML 61784-85). When a broker eventually complained on October 20, 2000, about Blodget's price objective and rating of the stock, Blodget contacted a fellow analyst: "[c]an we please reset this stupid price target and rip this piece of junk off whatever list it's on. If you have to downgrade it, downgrade it." (ML 06578). InfoSpace however, was not removed from the "Favored 15" until December 5, 2000 (ML 06700) and was not downgraded until December 11, 2000. (ML 00388; *see also* ML 61784-85)

Below is a chart of examples demonstrating discrepancies between the numerical investment ratings assigned by the Internet group and the group's contemporaneous internal analysis or opinions.

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3. Merrill Lynch Did Not Disclose The Analysts' Critical Conflicts of Interest

(a) The Internet Research group was not independent of investment banking

The evidence establishes that the Internet Research analysts were far from independent of their investment banking colleagues, and that their tortured relationship helped drive both the selection of covered stocks and the ratings ultimately assigned.

Tension between the various departments in a single firm is nothing new. At a securities firm, this tension is usually addressed by the establishment of a "Chinese Wall" – an internal relationship barrier by which investment bankers are prevented from sharing with other firm employees material, non-public information received by the bankers from their publicly-traded company clients. Thus, a banker generally should be barred from discussing such inside information with a research analyst who is disseminating to the public a research report on the same company. Another form of "Chinese Wall" attempts to prevent investment bankers from influencing analysts' ratings for the stock of existing or potential investment banking clients.

The compensation structure of a securities firm can exacerbate the potential for an analyst to be conflicted. Where analysts' compensation is affected, directly or indirectly, by the analysts' contribution to investment banking, analysts' objectivity and independence can be seriously eroded.

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Merrill Lynch's Policies and Procedures Manual for the Research Department (ML 02039, 02049) does not address the conflict raised by the compensation issue. Indeed, research analysts at Merrill Lynch were actively involved in evaluating and effectuating investment banking transactions. Moreover, analysts' compensation was tied to the success of their efforts in this regard.

The analysts in the internet group at Merrill Lynch knew very well that investment banking business translated into compensation for them personally and the firm generally, and that their research played a role in attracting and keeping that investment banking business. (ML 29830, ML 03806, ML 09544-51). In one revealing e-mail exchange, an analyst and investment banker discussed how to attract investment banking business of a company from a competitor. The banker proposed a formula that had apparently worked in the past with another banking client: "we should aggressively link coverage with banking - that is what we did with *Go2Net* (Henry [Blodget] was involved). . . . [I]f you are very bullish (b/c they will love you), they are not happy with GS [Goldman Sachs] and are going to be active, we can probably get by on a 'handshake.'" (ML 05229-30). This e-mail lays bare the understanding that Merrill Lynch intended the prospect of affirmative research to attract investment banking clients.

One way Blodget "prioritize[d]" research coverage for stocks was whether the company had an investment banking relationship with Merrill Lynch. (Blodget, Tr. at 207-08). Consistent with this agenda, Blodget, within weeks of joining Merrill Lynch as head of the Internet Research group,

distributed a memorandum entitled, "Managing the Banking Calendar for Internet Research," which he sent to the Co-Heads of U.S. Equity Research, and senior investment bankers. The memorandum unapologetically described Blodget's expectation that at least 50 percent of his and his team's time would be allocated to investment banking matters. In addition to discussing, "banking transactions [] in the pipeline" and "promising deals," the memorandum described Blodget's work schedule for one week as being divided "85% banking, 15% research." (ML 34660-61). Blodget's own time allocation reveals that Merrill Lynch viewed research as a sales tool for investment banking.

From December 1999 to November 2000, the Internet group was involved in investment banking deals that — on its own estimate — produced approximately $115 million of revenue to Merrill Lynch. The list of the group's activities for that year included participating in the bankers' sales pitch to potential clients; marketing transactions to institutional investors once the bankers had obtained the assignment; and then initiating and doing "follow-on" research coverage. This list is eight single-spaced pages long and contains scores of banking deals. (ML 09544-51, Campbell Tr. at 73-83).

The evidence examined to date confirms that the analysts' decisions about whether a stock should get coverage and what type of coverage it should receive were made neither objectively nor independent of the investment banking group. In one instance, an analyst stated that "part of the reason we didn't highlight [a risk] is because we wanted to protect ICG's banking business." (ML 60807). In another communication, an analyst worried about the impact of a particular rating on

the relationship with investment banking or its venture capitalists. (ML 60725). So pervasive was the tie between investment banking and research coverage, that when a competitor unexpectedly initiated coverage on the stock of a potential investment banking client, it prompted one Merrill Lynch analyst to respond, "they are angling for the M&A business too!" (ML 09032).

Analysts conveyed to one another that they would "win brownie points" from investment banking if the investment bankers could assure a company that the analysts would cover its stock. (ML 99103). Implicit in this was that "coverage" would always be favorable. Bankers, in turn, attempted to use the analysts to move the price of a stock to a level where research could be initiated, and so fulfill the promise of research coverage in exchange for banking work. One banker, who was frustrated by a stock's failure to reach the requisite price level of $10 before coverage could commence,[3] implored the Internet group to let the company speak at the group's upcoming conference that would be attended by many institutional investors — to promote Merrill Lynch's "active banking agenda" with the company and alleviate the company's unhappiness with the "research tie up" at Merrill Lynch. (ML29750).

Investment banking also was involved in criticizing and editing the Internet group's reports for client companies, opining on whether a particular rating would be acceptable

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3. Pursuant to a consent decree entered into with the Securities and Exchange Commission in the 1970's, Merrill Lynch is prohibited from initiating coverage on stocks trading below $10. (Abbott, Tr. at 84-85; ML 09151.) *See also* ML 02053.

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Company	Date	Contemporaneous Analyst Comments	Published Rating
Aether System (AETH)	03/15/01	"might have announcement next week . . . which could pop stock . . . but fundamentals horrible" (ML82578)	3-1
Excite @home (ATHM)	12/27/99 12/29/99	"we are neutral on the stock" Six month outlook is "flat", without any "real catalysts" for improvement seen (ML 37899; ML37956)	2-1
Excite @home (ATHM)	06/03/00	"such a piece of crap" (MLS 1453)	2-1
GoTo.Com (GOTO)	1/11/01	Nothing interesting about company "except banking fees" (ML03806)	3-1
InfoSpace (INSP)	7/13/00	"this stock is a powder keg, given how aggressive we were on it earlier this year and given the "bad smell" comments that so many institutions are bringing up (ML06413)	1-1

Company	Date	Contemporaneous Analyst Comments	Published Rating
InfoSpace (INSP)	10/20/00	"piece of junk" (ML06578)	1-1
Internet Capital Group Inc. (ICGE)	10/05/00	"Going to 5" (closed at $12.38) (ML63901)	2-1
Internet Capital Group Inc.(ICGE)	10/06/00	"No hopeful news to relate. . . . We see nothing that will turn this around near-term. The company needs to restructure its operations and raise additional cash, and until it does that, there is nothing positive to say." (ML64077)	2-1
Lifeminders (LFMN)	12/04/00	"POS" (piece of shit) (ML60903)	2-1
24/7 Media (TFSM)	10/10/00	"piece of shit" (ML 64372)	2-2

and, in at least one instance, apparently opposing a proposed rating because "[there is no] interest in seeing initiation [of research coverage] at a 3-2 [rating]." (ML 03799). Analysts openly discussed the conflict in e-mails, stating "the whole idea that we are independent front banking is a big lie — without banking this would be [rated] a 3-2." (ML 09045).

Research management itself acknowledged that "we are off base on how we rate stocks and how much we bend backwards to accommodate banking etc." (ML 64239). A host of e-mails demonstrate research management's knowledge and understanding of the conflicts, pressures, and confusion. *See, e.g.*, (ML 66935, ML 60847, ML 60865-66, ML 03607-08, ML 87610).

The conflicts and pressures that the research group experienced became particularly acute at the end of 2000 with respect to the mobile internist company, Aether Systems ("AETH"). As of September 27, 2000, Merrill Lynch was doing a secondary equity offering for the company, and the internet group was involved. (ML 09546). During what was supposed to be a confidential telephone conversation about the mobile internet sector, Merrill Lynch research analyst respondent Virginia Syer discussed Aether, InfoSpace ("INSP") and Phone.com ("PHCM"), but chose Phone.com — on which Merrill Lynch then had no coverage and to which it then provided no banking services — as having the "the best real business opportunity." (ML 63333-35, ML 09544-51). When the comments were e-mailed to a large number of recipients, Blodget chastised Eric Wellmann of Merrill Lynch's London office for "blast[ing] the contents out to the whole sales force". (ML 63333-35). Syer concurred, "it could

impair our relations w/those companies we do cover. We are marketing a big secondary for AETH [], and we were [banking] advisor in its sale to INSP. This is the sort of email that gets forwarded by a salesperson, and could very well get [] sent directly to any of these companies." The internet group's desire that accurate assessments be distributed to the public was clearly subservient to the desire to maintain investment banking's relationship with Aether.

Two months later, with Merrill Lynch fresh off the secondary offering of Aether, Syer drafted a downgrade of stocks in the mobile internet sector she covered, which included Aether, InfoSpace and Openwave ("OPWV"), from 1-1s to 2-1s, and forwarded the draft to research management, saying, "I want to be sure I am doing what research management wants here." She described four choices in handling the sensitive downgrade:

> First, we can downgrade to 2-1, and go out with the [draft] below. . . . Second, we can keep Aether at 1-1 . . . and downgrade OPWV and INSP for the reasons cited. (People would invariable [sic] ask the question why aren't we downgrading Aether.) Third, we can downgrade OPWV and INSP and say nothing about Aether. Fourth, we can keep them all at 1-1s and write press releases for research. (I sound flip but I am not being so — If banking is our top concern I'd just like us all to agree on it.)

(ML 06688).

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Andrew Melnick, a then head of Global Equity Research at Merrill Lynch, responded, "THE ONE CHOICE WE CANNOT DO IS DOWNGRADE THE OTHER COMPANIES AND LEAVE AETHER A 1-1. WE ARE NOT IN THE BUSINESS OF WRITING PRESS RELEASES." (ML 06688) (capital letters in original).

But Merrill Lynch did downgrade the others and left Aether at 1-1. On December 11, 2000, InfoSpace and Openwave were each downgraded to a 2-1. (ML 00384-87); Bloomberg News December 11, 2000 ("Openwave Systems cut to near-term 'accumulate' at Merrill") (ML 53507). Aether was not downgraded until February.

The Aether situation culminated in a general indictment by Blodget of the internet group's ratings. At the end of 2000, Blodget threatened to start to rate the stocks honestly, no matter what the investment banking consequences were. His ultimatum was prompted by a long-time broker who felt burned by late downgrades of covered stocks. (ML 68401-02), and an e-mail from research management regarding downgrades. Blodget wrote:

> The more I read of these, the less willing I am to cut companies any slack, regardless of predictable tamper-tantrums, threats, and/or relationship damage that are likely to follow.
>
> If you believe that this stance is a bad business decision for Merrill Lynch, please raise this with [senior management]. We all had to spend (waste) an unbelievable amount of time on the latest

> situation. . . . If there are no new email forthcoming from Andy [Melnick] on how the instructions below should be applied to sensitive banking clients/relations, *we are going to just start calling the stocks (stocks, not companies), including AETH, like we see them, no matter what the ancillary business consequences are.*

(ML 68401-02) (emphasis added). Thus, by Blodget's own admission, as late as the end of 2000, the internet group was *not* calling stocks as they saw them, but was permitting ancillary business consequences to taint their coverage.

Merrill Lynch has never publicly acknowledged the improper influence of investment banking on research. To the contrary, the public was specifically told that the internet group analysts were independent, objective and unbiased. (ML 85893; *see also* ML 02039, 02063). Knowing that such conflicts existed, and that members of the research group routinely acted as quasi-investment bankers, Merrill Lynch pretended there was a clear division, thereby enhancing the analysts' credibility. Thus, prior to the head of the Internet group appearing on television, he was reminded,

> CNN called and wanted to know if we are in AOL deal as an advisor. Head of media relations gave them a no comment. *If you are asked on Moneyline interview about that say something to the effect that you are not in the loop on that as you are in research not banking.*

(ML 41152) (emphasis added).

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(b) The analysts' compensation was linked to their investment banking work

The research analysts' objectivity and independence was further eroded by the fact that their compensation depended in part on their efforts on behalf of investment banking, as demonstrated by the following Fall 2000 request from respondent Deepak Raj, then co-head of global equity research, to all equity analysts:

> We are once again surveying your contributions to investment banking during the year. . . . Please provide complete details on your involvement in the transaction, paying particular attention the degree that your research coverage played a role in origination, execution and follow-up. Please note, as well, your involvement in advisory work on mergers or acquisitions, *especially where your coverage played a role in securing the assignment* and your follow-up marketing to clients. Please indicate *where your research coverage was pivotal in securing participation in high yield offering.*

On November 2, 2000, Blodget and the Internet Research group responded to the above request. In a detailed memorandum with schedules, entitled "IBK Contributions: Internet Team." Blodget stated that: (a) his group had been involved in over 52 completed or potential investment banking transactions; (b) the completed transactions had earned $115 million for the firm; and (c) more transactions would have been completed had not the "market window for most internet companies closed in June." He also identified

the services his analysts typically performed for investment banking, including pitching the client, marketing the offering and, notably, initiation and follow-on research coverage. (ML 09544-51; *see also* ML 33856). Shortly after documenting these contributions, Blodget's salary contract — which contained a guaranteed minimum — was cancelled and replaced with a substantially larger compensation package. Overall, Blodget's agreed-annual compensation, including "guaranteed" minimum cash bonus, increased from $3 million for 1999 to $12 million for 2001.

(c) The analysts were not independent from the companies they covered

The Internet group at times appeared more concerned with acting as consultants to the companies they covered than as objective analysts. For example, as the stock of InfoSpace plummeted, losing almost 90 percent of its value in a year, the Internet group counseled a senior officer of the company on how to handle himself and whether certain decisions were good business moves. (ML 06028). When the company's officer confided a plan to invest in a particular venture, the analyst gave investment banking advice:

> We need to talk about this. While I understand your genuine enthusiasm for the company and trust your "killer deal instinct", I am concerned that the market will not react favorable to any news that [InfoSpace] fund US Search. My BEST advice to you is to let Yahoo and Lycos win this one — there will be plenty of deals for you to do

> and [InfoSpace] cannot afford this kind of scrutiny right now — the stock is under a lot of pressure.

(ML 06424). Thus, as Merrill Lynch was supposedly providing the public with its objective opinion about a company's stock, it did not reveal that it was simultaneously advising that company how to keep the stock stable.

Merrill Lynch did not disclose to the public that the Internet group shared — and at times appeared even to negotiate — proposed ratings with the bankers and companies at issue, in clear violation of Merrill Lynch policy that analysts "may not disclose proposed investment conclusions" to company management. (ML 02054). Indeed, Blodget claimed not to even know of this prohibition. (KC 013). The results are intensely problematic: in one instance, a company agreed to a particular rating under the condition that its main competitor's stock would be downgraded to that same rating. It clearly violates Merrill Lynch's internal policies and illustrates that the subsequent ratings were biased when a company is given advance notice of its stock rating and a voice in a competitor's downgrade. (ML 09061). In another e-mail, an analyst reported that management of a company "do[es] not feel comfortable with us launching coverage of their stock . . . until [we] . . . [can] come out w[ith] a buy rating." (ML 63362). The internet group even contemplated giving coverage to a stock simply as an "accommodation for an important client," but only for six months, after which coverage would be dropped. (ML 36662).

The undisclosed influences manifested themselves in "support" for selected stocks. In one striking instance, an

internet analyst drafted a report on a company and shared it with Blodget, stating "trying to be oblique to help stock in anticipation of downgrade on wed[nesday]." (ML 43008). By failing to disclose the Internet group's candid appraisal of the stock's immediate prospects, Merrill Lynch deprived the public of necessary information. The deception inherent in the Internet group's ratings are the group's concerns for how their ratings and coverage would "impact . . . on the stock if we do a 3-1 so am leaning towards a 2-2 which is still our lowest rating," (ML 60723), or how they "may piss off" company management by writing what they really thought. (ML 63399).

(d) Misleading information was widely disseminated

The investment ratings of research were continuously made available to Financial Consultants — retail brokers — through Merrill Lynch's QRQ Opinion System. The system was designed to provide immediate access to the ratings by means of the broker's quote terminal; the information was also available in hard copy. When the retail broker pulled up a particular stock on the quote terminal, it showed the investment ratings, the stock price, any changes to the price and certain historical data such as price range, price/earnings ratio, and dividend. While other information about a company may have been available to the broker, such as flash notes and the research report, the broker was not required to consult it. Research Department's Policies and Procedures Manual, (ML 02052; ML 02083; Raj, Tr. at 164-89).

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Analysts also discussed recent research reports during a morning call apparently held before the market opened. Participation in the morning call was available to the Merrill Lynch institutional and retail sales forces. (Abbott, Tr. at 126-29). Research reports were also released on Merrill Lynch on-line system(s), which were available to Merrill Lynch clients and to third party vendors such as Bloomberg and First Call who made the reports available to subscribers who were entitled by Merrill Lynch to receive them. After a report had been released, institutional and retail clients and brokers who requested particular reports and had been "sponsored" (*i.e.*, a sales person or analyst paid the distribution cost) were e-mailed or mailed that particular report. *Id.*

Finally, research analysts discussed their opinions of stocks on appearances televised to the general investing public. For instance, in 1999 and 2000, Blodget appeared on television at least 77 and 46 times, respectively, often on CNBC and CNN. (March 4, 2002 letter of Andrew Kandell, Esq., Merrill Lynch, to Eric Dinallo, Esq., New York State Attorney General's Office).

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B. *Two Troubling Examples of Merrill Lynch's Treatment of Two Stocks*

1. GOTO.COM

a. Initiation of GoTo Coverage Was Linked to Banking Business

GoTo.com ("GoTo") (now known as Overture Services, Inc.) was an internet company, from which Merrill Lynch attempted and failed to obtain investment banking business in connection with its initial public offering ("IPO") in 1999. In 2000, Merrill Lynch again sought investment banking business from GoTo, in the form of a private placement offering for a European subsidiary of GoTo. The "pitch book" not only touted investment banking at Merrill Lynch but also heavily promoted Merrill Lynch's research analysts, including Blodget and his Internet group. (ML 17656-17657; ML 17709; ML 09279-80). By early September 2000, Merrill Lynch had received the mandate (*i.e.*, assignment) from GoTo for the European private placement, with the fee mostly contingent upon the private placement closing. (Mazzucco, Tr. at 325-26).

In connection with Merrill Lynch's obtaining this investment banking business, respondent Thomas Mazzucco, on behalf of Merrill Lynch investment banking, committed to Todd Tappin, Chief Financial Officer of GoTo, that Blodget would initiate research coverage of GoTo. (Tappan, Tr. at 100-03; OV 01102). When, in January 2001, Merrill Lynch initiated coverage of GoTo, an institutional investor e-mailed Blodget asking, "What's so interesting about GOTO except

banking fees????" Blodget responded, "nothin." (ML 03806). Blodget's candid response was not included in the initiation report, nor did the report disclose that Merrill Lynch had promised research coverage in exchange for GoTo's investment banking business.

b. The Initiation Process and Rating For GoTo Were Seriously Flawed

Shortly after Merrill Lynch received GoTo's mandate for the European private placement, Kirsten Campbell began working on a research report for initiation of coverage of GoTo. (Campbell, Tr. at 51, 57-61). In mid-September, she e-mailed GoTo financial models and a draft initiation report containing Merrill Lynch's proposed stock rating. Both the models and the draft report contained estimates and opinions, including Merrill Lynch's projections of GoTo's future financial performance. She specifically solicited the company's comments on the drafts and the company apparently provided them. (OV 270; OV 275).

As investment banking pressed for this co-operative drafting, (ML 30009-10), the internet group's objectivity and independence continued to be undermined. Campbell again e-mailed GoTo draft ratings, estimates and opinions in November, and again asked for comments which GoTo provided — including GoTo actually typing its changes into the draft initiation report, or in some sections, supplying the full text (OV 00182; OV 00248; OV 00257; OV 00295; OV 00301-02).

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In December, Campbell e-mailed a new financial model to GoTo, because she wanted it to "know we are cutting [GoTo's] revenue a lot," which would defer projected profitability out to the first quarter of 2003. (OV 01197). Russell Benaroya, GoTo's head of corporate development, e-mailed to Tappin and another colleague:

> "Based on these numbers, why would they even want to initiate on us. Todd [Tappin] should call back and pose that question. This is ridiculous and totally frustrating. Merrill will never take my company public."

(OV 01197). GoTo called Campbell and got its way: the final published initiation research report had profitability occurring sometime in 2002 rather than in the first quarter of 2003. (Tappin, Tr. at 127-29; ML 00404-08).

Disturbing discussions about the ratings were also occurring within Merrill Lynch. On November 16th Campbell e-mailed Blodget that she did not "want to be a whore for f-ing management" and initiate at a 2-2 (accumulate/accumulate) rating:

> if 2-2 means that we are putting half of merrill retail into this stock because they are out accumulating it then i don't think that's the right thing to do. We are losing people money and i don't like it. john and mary smith are losing their retirement because we don't want todd [Tappin, GoTo CFO] to be mad at us.

(ML 09045).

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Campbell also described in part her conversation with Mazzucco about a 3-2 (neutral/accumulate) initiation rating for GoTo. Although, according to Campbell, Mazzucco said he was "fine" with a 3-2, and that banking and research were independent of each other, Campbell responded:

> . . . the whole idea that we are independent from banking is a big lie — without banking this would be 3-2. . . .

Id.

In his sworn testimony, Blodget conceded that the Merrill Lynch investment bankers had veto power over his initiating coverage of GoTo with a 3 rating. (Blodget, Tr. at 211-12). Although apparently agreeing to the neutral intermediate rating, investment banking prevailed in that the rating would be a 3-1 (neutral-buy) and not the 3-2 (neutral-accumulate) that Campbell said would be appropriate but for investment banking's pressure. Hence, on November 21st, Campbell e-mailed Blodget:

> *goto* has gotten back to me and says they are "comfortable" with the discussions we've had with them, and with coming out at a 3-1 etc. given that we would be downgrading LOOK [GoTo's business competitor] at the same time so the ratings are the same . . .

(ML 09061). In the same e-mail, Campbell also informed Blodget that she had consulted with their research colleague, respondent Justin Baldauf, who covered Looksmart, and that

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Baldauf was not convinced that downgrading Looksmart was a good idea because there was "no reason to do now versus before." *Id.*

Although the plan to downgrade Looksmart made Merrill Lynch's proposed 3-1 initiation rating on GoTo sufficiently palatable to GoTo. GoTo's Benaroya expressed concern that a *simultaneous* Looksmart downgrade might attract unwanted attention:

> I don't know if we have to have simultaneous GoTo/Look notes. Wouldn't that be a bit strange? You could probably initiate on GoTo first and come out with a LOOK note soon thereafter. Let me know.

(ML 35973-74). Campbell's response was "re: LOOK – no it wouldn't be strange." *Id.*

Blodget, in an e-mail to Baldauf, confirmed his intention to simultaneously initiation GoTo and downgrade Looksmart "we are going to cut numbers for q1 and q2 and roll with a 3-1 on GoTo, would like to do the same for LOOK if it makes sense. . . ." (ML 09145). Blodget further confirmed the plan on December 19, 2000, when he e-mailed Campbell and Baldauf:

> K,
> Here's the GoTo note.
> Justin, We're planning to roll on this thing on Thursday at 3-1. I'd like to take the LOOK rating to 3-1 at the same time, just so we can keep them

> together. Probably easiest if we just cut the numbers a bit again to be conservative. Let me know your thoughts.

(ML 36007).

On December 20th, initiation at the agreed upon 3-1 ran into a stumbling block: the GoTo stock price was below $10. On January 4, 2001, Campbell e-mailed the investment bankers, Mazzucco and Andrew Siegel, research management wanted to initiate coverage with a 3-2 (neutral/accumulate) on *GOTO*." (ML 3799). Siegel vigorously opposed the 3-2 rating in a reply to Blodget and Campbell:

> Please listen to my VM [voice mail] from this morning. Briefly, in talking to Ray Abbott [head of compliance] yesterday, I thought the strategy was to go out with the 3-1 as soon as the stock hit $10; if it doesn't, I don't think anybody has an interest in seeing initiation at 3-2.

Id.

Blodget's immediate response was his "concern . . . that waiting for $10 is waiting for Godot. . . ." *Id.* When the stock didn't hit $10 the next day, Mazzucco asked a research analyst if she would arrange for GoTo to have an opportunity to promote itself at an upcoming conference of institutional investors. (ML 29750). The GoTo stock finally traded intra-day at $10 on January 10th, and Blodget initiated coverage

the next day at the 3-1 rating acceptable to the investment bankers and GoTo. (ML 00404 - 08).

The final research initiation report for GoTo that was submitted to research compliance described Looksmart as rated at 3-1. Not surprisingly, compliance crossed out the 3-1 and wrote 2-1, the rating Looksmart still enjoyed as of that date. (ML 00709-18). The final research report for Looksmart, issued later that day, affected the downgrade from 2-1 to 3-1, just as GoTo had been promised. (ML 26324-25).

c. Investment Rating Downgrade of GoTo

On April 25, 2001, Blodget and respondent Ed McCabe[4] (a senior analyst who reported to Blodget) upgraded GoTo to a 2-1 (accumulate-buy) rating. (ML 00585-88). On May 16th and 17th, 2001, Blodget and the investment bankers sponsored an investor road show for GoTo's CEO and CFO, after which GoTo's stock rose 20 percent. (ML 04058; ML 29677-78; OV 00217-18).

In May 2001, Mazzucco suggested to GoTo's Tappin the possibility of an equity offering by GoTo, and a meeting was set for May 31st for GoTo and Merrill Lynch to discuss this and other investment banking-related issues. (ML 08737; ML 18489-90). At about the same time, Mazzucco spoke with the CFO of idealab, GoTo's largest stock holder, (Mazzucco, Tr. at 326-30), about the possibility of monetizing idealab's GoTo stock, and that the CFO would "be pitching us as his

4. In mid-April, 2001, Campbell left Merrill Lynch and was replaced on the GoTo research coverage by McCabe.

first choice" for such a transaction. (ML 29680). In the meantime, Blodget continued to publish bullish research reports on GoTo. (ML 00639-42; ML 00643-44).[5]

On May 25th, GoTo's CEO Ted Meisel and Tappin advised Mazzucco that GoTo had decided to proceed with an equity offering, but that the company was leaning towards Credit Suisse First Boston ("CSFB") as the lead book running manager instead of Merrill Lynch.[6] (ML 29644, Exhibit 246). This would prevent Mazzucco from having Merrill Lynch participate in any way in the underwriting of the offering, given the technology group's policy requiring Mardi Lynch to be a book runner manager. Upset at this sudden, adverse turn of events, Mazzucco on the same day drafted an e-mail to be sent to the Chairman and Vice-Chairman of idealab, and the manager/general partner of idealab Capital Partners, all of whom were also Directors of GoTo:

> I spoke with Ted Meisel and Todd Tappin [GoTo's CEO and CFO] today and they informed me of their decision to proceed with an offering of stock

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5. Mazzucco emailed a copy of this research report to the CFO of idealab, commenting: "In it Henry [Blodget] highlights the outlook for the Internet advertising market and reiterates GoTo as a focus stock." (ML 29649-52).

6. The book runner manager of a public offering controls the stock allocations to investors. Being a book runner manager was so important to Merrill Lynch that during the relevant period, its investment banking technology group had an "informal" policy that barred the group from being an underwriter unless it was a book runner manager. (Mazzucco, Tr. at 373-74).

> from both idealab! and GoTo. We think it is a terrific idea and one that we have brought up with them over the past few weeks. I was very dismayed to learn that they were leaning toward CSFB as the lead book running manager, particularly given the tremendous effort we have put forth on the Company's behalf. Not only did Henry Blodget show leadership by initiating on the stock near its low point but he recently upgraded it and sponsored a set of investor and Merrill sales force meetings for management in New York, which dramatically moved the stock price . . . As book running manager, I am confident that we are best position to ensure that execution and therefore deliver for both GoTo and Idealab!. An alternative structure would be Merrill Lynch and CSFB as joint book-running managers . . . Your support would be most appreciated. . . . (Exhibit 246) (Mazzucco, Tr. at 383-86, 395-400)

Almost simultaneously, within the Internet group, McCabe e-mailed Blodget a draft downgrade of GoTo's stock from its then current 2-1:

> **H,**
> **I don't think I've downgraded a stock on valuation since the mid-90's. Anyway, I threw together these bullets in a note on my hard drive so that we are ready to pull the trigger quickly. Do you think we need more than bullets? I didn't think so since this downgrade would be based solely on valuation? Let me know.**
> **Thanks.**
> **Ed**

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> • ***GoTo* has doubled since our upgrade about a month ago. We are downgrading the stock due to valuation.**
>
> • **We believe fundamentals are intact . . .**

(ML 04097) (emphasis in original).

Blodget's immediate three-word reaction was: "beautiful fuk em." *Id.*

But if valuation concerns truly were driving the downgrade, the timing was inexplicable. The GoTo stock closing price on May 25th was $22.75 — virtually the same as the price of $23 at which Blodget in the two earlier research reports — May 22nd and May 23rd — had recommended the stock with a bullish 2-1 rating. (ML00639-42; ML 00643-44).

The downgrade was not issued, but held in reserve as Merrill Lynch continued to lobby to be book running manager. (Mazzucco, Tr. at 375-81). On May 29th Mazzucco and Siegel placed GoTo's equity offering on Merrill Lynch's Grey Scan system, to note Merrill Lynch's pursuit of that banking deal. (Abbott, Tr. at 283-84, ML 02022-24). However, on the evening of May 29th, Mazzucco e-mailed Siegel that he had just learned GoTo had decided to retain CSFB as sole book running manager, and that the May 31st banking meeting with GoTo was off (ML 29643). Further, Siegel's calendar for June 1st states: "Take GoTo off greylist for follow-on," (ML 28908), and in fact Merrill Lynch did not participate as an underwriter in the offering.

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On the morning of June 6th Blodget was alerted that GoTo had announced the filing of its SEC registration statement for a proposed offering of 2,500,000 shares plus a resale of 5,000,000 shares held by idealab. CSFB was the book running manager and lead underwriter of the offering. (Exh. 46). Merrill Lynch thus had lost the underwriting for the equity offering, the opportunity to monetize GoTo stock of idealab, and the chance for other business from the now-cancelled May 31st meeting. Moreover, the European private placement of almost a year earlier had never come to fruition. (Mazzucco, Tr. at 331-33; ML 29643).

Within an hour of the announcement of the equity offering, research compliance received the proposed downgrade of GoTo that McCabe had sent Blodget on May 25th, with minor changes. Ray Abbott, head of research compliance, testified that McCabe claimed that Blodget and McCabe had been watching the GoTo stock price for several days, that the stock had exceeded their published price objective, that they were looking for an event which might cause the stock to trend downward, and that the announcement of the GoTo offering was precisely such an event. (Abbott, Tr. at 319-21;413-16). By mid-morning on June 6th, the Blodget downgrade of GoTo from 2-1 to 3-1 was released to the public in substantially the same form that had elicited Blodget's enthusiastic and blunt reaction on May 25th.

Although the downgrade purportedly resulted from the increased stock price and the announcement of the equity secondary offering, the downgrade tellingly makes no mention of the equity offering, much less that the offering

would drive the GoTo stock price down. (ML00649-50). McCabe explicitly recognized this contradiction in an e-mail he sent to Blodget two days after the downgrade: "just had to explain to a client we didn't *downgrade* due to offering." (ML 04124) (emphasis in original). Finally, Abbott conceded that if he had seen Blodget's May research report recommending GoTo with a robust 2-1 rating at a price of $23 — which was already 21 percent above Blodget's published price objective — "it should have raised a red flag" about the downgrade. (Abbott, Tr. at 363-65).

2. INFOSPACE

Merrill Lynch initiated coverage of InfoSpace in December 1999 with a rating of 2-1 (accumulate-buy) and a price objective of $160. The stock then traded at $152.50. Shortly thereafter, Merrill Lynch upgraded the rating to 1-1. As of March 2, 2000, the price had reached $261, but thereafter the stock steadily dropped. Yet Merrill Lynch's Internet group maintained a 1-1 rating on the stock to December 10, 2000, when the price was $13.69.[7] No sell rating was ever issued.

Throughout 2000, Merrill Lynch strongly supported InfoSpace. By March 21, 2000, it had upgraded its rating to a 1-1 (buy-buy), even though the stock was down considerably from its high, and concerns about the company's accounting practices had surfaced. The price objective nevertheless was then at $200. (ML 00002).

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7. From December 1999 to December 2000, the stock split twice, each time at two for one.

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Around this time, Merrill Lynch was courting investment banking business from Go2Net, a technology company. On an April 5, 2000 conference call, Blodget and Mazzucco gave Go2Net, a "presentation" about Merrill Lynch's investment banking and research abilities. In written materials, Blodget was promoted with a photograph and InfoSpace was listed as one of Merrill Lynch's covered stocks. (ML 09260-61; ML 09279-80).

While the Internet group continued to promote InfoSpace stock with buy/buy ratings, Merrill Lynch brokers began to raise numerous and serious questions about Merrill Lynch's support of the stock in e-mails to Blodget and respondent Sofia Ghachem between April and July: "What is the deal with InfoSpace . . . [I] feel reluctant to push it these days," (ML 05795) "should we be concerned about this . . . InfoSpace reported a loss of 38 cents a share, compared to a loss of 3 cents per share a year ago. . . ." (ML 05902) and "the stock continues to underperform and . . . few mutual fund managers are buying this stock . . . maybe we should re-evaluate our stance, i am really concerned for our clients." (ML 06230). Ghachem also was questioned about InfoSpace's management selling their shares of the stock. (ML 06228-29).

By June 1, 2000, the stock price had fallen to $43, but Merrill Lynch continued its buy/buy ratings. (ML 00049-50). On June 15, 2000, Blodget e-mailed Ghachem, confessing "enormous skepticism" about the stock. (ML 06257-58). On June 20, Ghachem e-mailed Blodget to inform him that investment banking was meeting with InfoSpace on June 27th and the bankers had promised InfoSpace that Blodget would appear. (ML 06334).

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Merrill Lynch's buy ratings continued into early July 2000. On July 10, 2000, Go2Net went on Merrill Lynch's Grey Scan list, because Go2Net had asked Merrill Lynch to undertake a sale of Go2Net to InfoSpace. (ML 02026-27). The next day, Merrill Lynch issued a "company update" — commonly referred to as a "booster shot" – on InfoSpace reiterating its buy rating. (ML 00068-69). Unlike several other company updates on InfoSpace, no discernable reason was given for the update. In mid July, Blodget complained to Ghachem, "I'm getting killed on this thing," (ML 06417), yet his buy ratings for InfoSpace continued, even as the stock dropped further in price.

On October 26, 2000, Merrill Lynch completed the sale of Go2Net to InfoSpace. (ML 02027). On December 11, 2000, Merrill Lynch finally reduced its rating to accumulate; the price had hit $13. On December 20, 2000, Merrill Lynch issued a research bulletin indicating that InfoSpace's Vice-President had filed a lawsuit against InfoSpace's CEO, alleging multiple securities violations and racketeering. (ML 00384-87; ML 00397).

From July 2000 through April 2001, e-mails reflect tremendous doubts by the Merrill Lynch analysts as to the future of InfoSpace and the ethics of its CEO. While Merrill Lynch's rating sat at 1-1 with a price objective of $100, its analysts graphically observed that the stock "is a piece of junk" and "toast" if the CEO leaves. (ML 06578; ML 6407-08). When a Merrill Lynch broker wrote to Blodget commenting on InfoSpace's poorly written 1999 annual report. Blodget responded, to Ghachem that he "would love to reset the price target to $30 or something." (ML 06577).

Even after Merrill Lynch finally downgraded the stock to 2-1 in December of 2000, the stock still enjoyed an "accumulate" rating, despite the Internet group's frank internal comments about "what a sleazebag" the CEO was and how Blodget now was "officially not comfortable" with the CEO being associated with the company. (ML 00397; ML 06769-70; ML 06771-72).

The evidence suggests that business considerations influenced the Internet group in maintaining its buy rating for InfoSpace as long as it did. The group regarded InfoSpace important to Merrill Lynch's banking business, as evidenced by a May 17, 2000 e-mail to a member of the Merrill Lynch retail staff:

> This company [InfoSpace] is very important to us from a banking perspective, in addition to our institutional franchise. . . .

(ML 48862) (adding that "non-deal roadshows" for companies such as InfoSpace "have a tremendous effect on our banking efforts).

III. NECESSITY OF THE SECTION 354 ORDER

The foregoing summary of some of the evidence gathered by the Attorney General's investigation to date pursuant to GBL § 352 demonstrates that profoundly troubling questions pervade Merrill Lynch's research and rating system, as that system has been employed by the company's Internet group. Contrary to the image of objectivity that Merrill Lynch has sought to cultivate for its research arts, the evidence shows

that analysts knowingly compromised their honestly held beliefs regarding the merits of particular stocks and skewed the ratings they issued in order to promote the interests of Merrill Lynch's investment banking business, and that the analysts' involvement in that business netted them substantial monetary rewards. The investing public, of course, knew nothing of the inherent conflict of interest underlying the Merrill Lynch rating system, and was deprived of the analysts' honest opinions.

The Attorney General is charged with the responsibility of investigating the commission of fraudulent practices by securities promoters and has authority, under GBL §353, to bring a plenary action on behalf of the public to seek redress and to enjoin entities and individuals from, *inter alia*, committing fraudulent practices, ever directly or indirectly engaging or participating in the issuing, offering or selling of securities, or providing investment advice, within or from the State of New York. The Attorney General also may prosecute Martin Act violations criminally under GBL §352-c.

Section 354 provides that once the Attorney General has decided to commence an enforcement action under the Martin Act, he may apply to the Court for preliminary relief and judicial supervision of the continued gathering of evidence. At this stage in the investigation, the Attorney General has determined that such action is appropriate and shall be commenced against the respondents. The testimony and documents requested are material and necessary for the Attorney General to establish the full scope of the Martin Act violations revealed by the investigation to date. However,

the public and the community of securities regulators need not, and should not, await the outcome of the Attorney General's investigation before they can receive preliminary relief and address the serious problems exposed by the record amassed to date.

Potential purchasers of securities are entitled to both a complete investigation of this matter and immediate injunctive relief. Unless the application herein is granted, the investing public will be deprived of knowledge and safeguards vital to the integrity of our securities industry. Accordingly, pending further development of the record, respondents should be restrained and enjoined in the manner set forth in the proposed order submitted herewith.

The Attorney General intends to continue his investigation and examine the conduct of other major participants in the securities industry. To this end, several other investment banks currently are under Martin Act subpoena to produce evidence regarding their stock research and ratings function. The Attorney General anticipates that after the evidence sought has been produced and studied further application to this Court may be warranted for broader public investigation and eventual relief.

WHEREFORE, the Attorney General respectfully requests that this Court grant the within application for an Order pursuant to GBL Section 354, with the accompanying injunctive relief, in the form annexed hereto, and for such further and other relief as the Court may deem just and proper.

Eric R. Dinallo, Assistant Attorney General

Appendix F

News from
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For immediate release:
April 8, 2002

MERRILL LYNCH STOCK RATING SYSTEM FOUND BIASED BY UNDISCLOSED CONFLICTS OF INTEREST

Spitzer Obtains Court Order Requiring Key Disclosure

State Attorney General Eliot Spitzer today announced a court order requiring immediate reforms in investment counseling by one of the nation's oldest and largest securities films.

The court action against Merrill Lynch was the result of an investigation by Spitzer that concluded that the firm's supposedly independent and objective investment advice was tainted and biased by the desire to aid Merrill Lynch's investment banking business.

Spitzer cites dramatic evidence that the firm's stock ratings were biased and distorted in an attempt to secure and maintain lucrative contracts for investment banking services. As a result, the firm often disseminated misleading information that helped its corporate clients but harmed individual investors.

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"This was a shocking betrayal of trust by one of Wall Street's most trusted names," Spitzer said. "The case must be a catalyst for reform throughout the entire industry."

Spitzer's office uncovered a major breakdown in the supposed separation between the banking and research divisions at Merrill Lynch. In fact, analysts at Merrill Lynch helped recruit new investment banking clients and were paid to do so. The public, however, was led to believe that research analysts were independent, and that the firm's rating system would assist them in making critical investment decisions.

As part of a quid pro quo between the firm and its investment banking clients, Merrill Lynch analysts skewed stock ratings, giving favorable coverage to preferred clients, even when those stocks were dubious investments.

This problem and other conflicts of interest are revealed by internal e-mail communications obtained during the investigation by the Attorney General's office.

These communications show analysts privately disparaging companies while publicly recommending their stocks. For example, one analyst made highly disparaging remarks about the management of an internet company and called the company's stock "a piece of junk," yet gave the company, which was a major investment banking client, the firm's highest stock rating.

The communications show analysts complaining about pressure from Merrill Lynch's investment banking division. For example, a senior analyst writes: "the whole idea that we are independent of (the) banking (division) is a big lie."

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A senior manager stated: "We are off bases in how we rate stocks and how much we bend over backwards to accommodate banking." But nothing was done to remedy this fundamental problem.

The communications show that the problems at Merrill Lynch went far beyond a single analyst or research unit. For example, the head of the equity division wrote to analysts: "We are once again surveying your contribution to investment banking . . . please provide complete details on your involvement . . . paying particular attention to the degree your research played a role in originating. . . . <banking business.>"

And most importantly, the communications show how individual investors were harmed. A research analyst complained about giving a buy rating to a poor investment: "I don't think it is the right thing to do. John and Mary Smith are losing their retirement because we don't want a client's CEO to be mad at us."

The court order obtained by Spitzer requires Merrill Lynch to now make disclosures to investors about its relationship with investment banking clients and provide more context for its stock ratings.

Spitzer described the court order as a preliminary step designed to protect investors while the investigation continues. He said his office has issued subpoenas to other securities firms. The nearly year long investigation is being handled by the Attorney General's Investment Protection Bureau, under the direction of Assistant Attorney General Eric Dinallo.

APPENDIX G — TRANSFER ORDER DATED OCTOBER 11, 2002

RELEASED FOR PUBLICATION

DOCKET NO. 1484

BEFORE THE JUDICIAL PANEL ON MULTIDISTRICT LITIGATION

IN RE MERRILL LYNCH & CO., INC., RESEARCH REPORTS SECURITIES LITIGATION

BEFORE WM. TERRELL HODGES, CHAIRMAN, JOHN F. KEENAN, MOREY L. SEAR,* BRUCE M. SELYA, JULIA SMITH GIBBONS, D. LOWELL JENSEN AND J. FREDERICK MOTZ, JUDGES OF THE PANEL

TRANSFER ORDER

This litigation presently consists of 43 actions: 39 actions in the Southern District of New York; and one action each in the District of New Jersey, the Western District of Oklahoma, the Western District of Texas, and the Western District of Washington.[1] Before the Panel is a motion, pursuant to

* Judge Sear took no part in the decision of this matter.

1. The Panel has been notified that 80 potentially related actions have been filed: 51 actions in the Southern District of New York; three actions each in the District of Arizona, the Northern District of California, and the Northern District of Texas; two actions each in the Central District of California, the Middle District of Florida, the Eastern District of Michigan, the District of Minnesota, the (Cont'd)

28 U.S.C. § 1407, by defendants Merrill Lynch & Co., Inc., and Merrill Lynch, Pierce, Fenner & Smith Inc. (Merrill Lynch) to centralize these actions in the Southern District of New York for coordinated or consolidated pretrial proceedings. Nearly all responding parties support Section 1407 centralization of claims against the Merrill Lynch defendants in a single federal court, but disagree on the most appropriate transferee district. In addition to the Southern District of New York, responding parties suggest selection of the Western District of Oklahoma or the District of Minnesota as transferee district. The *InfoSpace, Inc.* (*InfoSpace*) defendants in the Western District of Washington action (*InfoSpace*) along with several other parties oppose inclusion of claims against the *InfoSpace* defendants in MDL-1484 proceedings and ask the Panel to sever and simultaneously remand these claims to the Washington federal court. The *InfoSpace* plaintiffs oppose inclusion of their action in MDL-1484 proceedings, oppose severance and remand of the claims against the *InfoSpace* director/officer defendants, and ask the Panel to transfer one New York action to the Western District of Washington. Some additional responding plaintiffs also oppose inclusion of their action or potential tag-along action in MDL-1484 pretrial proceedings.

(Cont'd)
Southern District of Mississippi, and the District of New Jersey; and one action each in the Southern District of California, the Northern District of Illinois, the Western District of Kentucky, the District of Maryland, the District of Oregon, the Middle District of Pennsylvania, the Southern District of Florida, and the Western District of Tennessee. These actions and any other related actions will be treated as potential tag-along actions. *See* Rules 7.4 and 7.5, R.P.J.P.M.L., 199 F.R.D. 425, 435-36 (2001).

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On the basis of the papers filed and hearing session held, the Panel finds that the actions in this litigation involve common questions of fact, and that centralization under Section 1407 in the Southern District of New York will serve the convenience of the parties and witnesses and promote the just and efficient conduct of the litigation. All actions share factual questions arising out of allegations that i) from 1999 through 2001, Merrill Lynch and various individually named related defendants issued false and misleading analyst reports concerning publicly traded securities of primarily internet companies in order to promote business for Merrill Lynch's investment banking division, and ii) Merrill Lynch failed to disclose this conflict of interest between its research and investment banking divisions. Centralization under Section 1407 is thus necessary in order to eliminate duplicative discovery, prevent inconsistent pretrial rulings (especially with respect to questions of class certification), and conserve the resources of the parties, their counsel and the judiciary.

Several parties urge the Panel to include the *InfoSpace* action in MDL-1484 pretrial proceedings and to sever and simultaneously remand claims against the *InfoSpace* defendants to the Western District of Washington. The *InfoSpace* plaintiffs oppose this request primarily on the ground that this action includes allegations that the *InfoSpace* defendants conspired with the Merrill Lynch defendants to mislead investors. The presence of conspiracy allegations in *InfoSpace* is debatable and we are reluctant, on the record now before us, to make a determination that claims in *InfoSpace* are severable. It may be, on further refinement of the issues and close scrutiny by Judge Milton Pollack, that

claims against the *InfoSpace* defendants can be remanded to the Western District of Washington for further proceedings in advance of claims against the Merrill Lynch defendants. Should Judge Pollack deem Section 1407 remand of any claims appropriate, procedures are available whereby this may be accomplished with a minimum of delay. *See* Rule 7.6, 199 F.R.D. at 436-38. In any event, transfer of all claims in all actions to a single district under Section 1407 has the salutary effect of placing all the related actions before a single judge who can formulate a pretrial program that: 1) allows pretrial proceedings with respect to any non-common issues to proceed concurrently with pretrial proceedings on common issues, *In re Multi-Piece Rim Products Liability Litigation*, 464 F. Supp. 969, 974 (J.P.M.L. 1979); and 2) ensures that pretrial proceedings will be conducted in a manner leading to the just and expeditious resolution of all actions to the overall benefit of the parties. We are confident in Judge Pollack's ability to streamline pretrial proceedings in all actions, while concomitantly directing the appropriate resolution of all claims.

Although any of the suggested federal districts would be an appropriate forum for Section 1407 proceedings in this litigation, the Panel has decided to entrust this litigation to the Southern District of New York, where 39 constituent actions and 51 potential tag-along actions are pending. We note that this district i) is conveniently located for many parties and witnesses, and ii) possesses the necessary resources to be able to devote the substantial time and effort to pretrial matters that this complex docket is likely to require.

Appendix G

IT IS THEREFORE ORDERED that, pursuant to 28 U.S.C. § 1407, the actions listed on the attached Schedule A and pending outside the Southern District of New York are transferred to the Southern District of New York and, with the consent of that court, assigned to the Honorable Milton Pollack for coordinated or consolidated pretrial proceedings with the actions pending there,

FOR THE PANEL:

s/ Wm. Terrell Hodges
Wm. Terrell Hodges
Chairman

Appendix G

SCHEDULE A

MDL-1484 — In re Merrill Lynch & Co., Inc., Research Reports Securities Litigation

District of New Jersey

William C. Ciemny v. Merrill Lynch, Pierce, Fenner & Smith, Inc., et al., C.A. No. 1:02-2576

Southern District of New York

In re Merrill Lynch InfoSpace Analyst Reports Securities Litigation, C.A. No. 1:01-6881

Sandra Blair, et al. v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3042

Lou A. Murphy v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3050

Aaron Priest v. Merrill Lynch & Co., Inc., et. al., C.A. No. 1:02-3189

Abraham Twersky Family Trust v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3210

Jack B. McBride v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3252

John Deleo v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3321

Leonard Corwin v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3366

Roger Matthews, et al. v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3371

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Dwight Corkins v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3372

Jason Silver v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3394

Jon M. Rosenbaum v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3410

James Crowdus v. Merrill Lynch & Co. Inc., et al., C.A. No. 1:02-3417

Sanjay Israni v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3418

Frank J. Vonder Haar v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3429

Harold Ducharme v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3431

Bernd Toennesmann v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3466

Michael M. Moore v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3509

Wayne Boyce v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3510

Ira Atlas v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3513

David Foushee v. Merrill Lynch & Co., Inc., et at., C.A. No. 1:02-3599

Giuseppe Coppola v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3600

Steven Wald v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3606

Bernd Toennesmann v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3634

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Turgut Ergun v. Merrill Lynch & Co., Inc., et al., C.A. No. 1.02-3675

Daniel R. Gerrity v. Merrill Lynch & Co., Inc., et al., C.A. No. *1:02-3690*

Doug Seindenburg v. Merrill Lynch & Co. Inc., et al., C.A. No. 1:02-3714

Paul Hesano v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3715

Robert Rueben v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3759

Victor Parker, etc. v. Merrill Lynch & Co., Inc., et al., C.A. *No.* 1:02-3835

Jason Cho v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3882

Fredell D. Williams v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3934

Seth B. Marks v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-3975

Elisha Ciccarelli v. Merrill Lynch Co., Inc., C.A. No. 1:02-4051

Dean E. Hart v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-4058

Stephen A. McKernan v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-4140

Steven Smith v. Merrill Lynch & Co., Inc., C.A. No. 1:02-4205

J. James Walsh v. Merrill Lynch & Co., Inc., et al., C.A. No. 1:02-4228

Samuel Sinay, et al. v. Merrill Lynch & Co., Inc., et at, C.A. No. 1:02-4237

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Western District of Oklahoma

Shadi Dabit v. Merrill Lynch, Pierce, Fenner & Smith, Inc., C.A. No. 5:02-564

Western District of Texas

William A. Clearly v. Merrill Lynch Securities, C.A. No. 5:02-364

Western District of Washington

John Horton, et al. v. InfoSpace Inc., et al., C.A. No. 2:01-913

No. 04-1371

Supreme Court, U.S.
FILED
NOV 14 2005
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

MERRILL LYNCH, PIERCE, FENNER & SMITH, INC.,

Petitioner,

v.

SHADI DABIT, on behalf of himself and all others similarly situated,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR PETITIONER

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QUESTION PRESENTED

Whether the Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227, preempts state law "holder" class actions brought on behalf of persons who assert that they were induced by allegedly fraudulent statements or omissions to hold (*i.e.*, refrain from selling), as opposed to purchase or sell, securities?

STATEMENT PURSUANT TO RULE 29.6

Petitioner's corporate disclosure statement was set forth at page ii of its Petition for a Writ of Certiorari. There are no amendments to that statement.

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B. This Court has broadly construed the "in connection with" language of section 10(b) that is imported into SLUSA's preemption provision. 24

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II. Importing into SLUSA the Purchaser-Seller Standing Limitation Would Frustrate Congress' Purpose and Lead to an Absurd Interpretation of the Statute. 33

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